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DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

7 CFR Part 1210

[Document Number AMS–SC–19–0109]

Watermelon Research and Promotion Plan; Realignment

AGENCY: Agricultural Marketing Service.

ACTION: Final rule.

SUMMARY: This rule realigns the representation on the National Watermelon Promotion Board (Board) under the Agricultural Marketing Service's (AMS) regulations regarding a national research and promotion program for watermelons. This rule reduces the number of production districts and the number of importers on the Board, accordingly. This rule also makes administrative changes to other provisions of the Watermelon Research and Promotion Plan (Plan).

DATES: Effective October 14, 2020.

FOR FURTHER INFORMATION CONTACT: Stacy Jones King, Agricultural Marketing Specialist, Promotion and Economics Division, Specialty Crops Program, AMS, USDA, 1400 Independence Avenue SW, Room 1406–S, Stop 0244, Washington, DC 20250–0244; telephone: (202) 731–2117; facsimile: (202) 205–2800; or electronic mail: *Stacy.JonesKing@usda.gov.*

SUPPLEMENTARY INFORMATION: This final rule affecting 7 CFR part 1210 is authorized under the Watermelon Research and Promotion Act (Act) (7 U.S.C. 4901–4916). The Watermelon Research and Promotion Plan is codified at 7 CFR part 1210.

Executive Orders 12866, 13563, and 13771

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, reducing costs, harmonizing rules and promoting flexibility. This final rule falls within a category of regulatory actions that the Office of Management and Budget (OMB) exempted from Executive Order 12866 review. Additionally, because this rule does not meet the definition of a significant regulatory action it does not trigger the requirements contained in Executive Order 13771. *See* OMB's Memorandum titled ''Interim Guidance Implementing Section 2 of the Executive Order of January 30, 2017, titled 'Reducing Regulation and Controlling Regulatory Costs' '' (February 2, 2017).

Executive Order 13175

This final rule has been reviewed in accordance with the requirements of Executive Order 13175, Consultation and Coordination with Indian Tribal Governments. The review reveals that this rule will not have substantial and direct effects on Tribal governments and will not have significant Tribal implications.

Executive Order 12988

This rule has been reviewed under Executive Order 12988, Civil Justice Reform. It is not intended to have retroactive effect.

Under section 1650 of the Act (7 U.S.C. 4909), a person subject to an order may file a written petition with USDA stating that the plan, any provision of the plan, or any obligation imposed in connection with the plan, is not established in accordance with the law, and request a modification thereof or an exemption therefrom. The petitioner will have the opportunity for a hearing on the petition. Thereafter, USDA will issue a ruling on the petition. If the petitioner disagrees with USDA's ruling, the petitioner may file, within 20 days, an appeal in the U.S. District Court for the district where the petitioner is an inhabitant or in which the person's principal place of business is located.

Background

This rule realigns the Board's representation and procedures under the Plan. The realignment reduces the number of production districts under the Plan for producer and handler representation on the Board, and proportionally reduces the number of importer seats from twelve to nine. The Board administers the Plan with oversight by USDA. Under the Plan, assessments are collected from watermelon producers, handlers and importers. The assessments are used to strengthen watermelon's position in the marketplace and to establish, maintain, and expand markets for watermelons.

Board Membership

Currently, § 1210.320(a) specifies that the Board shall be comprised of producers, handlers, importers and one public representative appointed by the Secretary. Pursuant to § 1210.320(b), the Plan originally divided the United States into seven districts of comparable production volumes of watermelons, and each district is allocated two producer members and two handler members. Section 1210.320(d) specifies that importer representation on the Board shall be proportionate to the percentage of assessments paid by importers to the Board, except that at least one representative of importers shall serve on the Board.

The current Board is comprised of 41 members—14 producers (two from each district), 14 handlers (two from each district), 12 importers, and one public member.

Review of U.S. Production

Section 1210.320(c) requires the Board, at least every five years, to review the districts to determine whether realignment is necessary. In conducting the review, the Board must consider: (1) The most recent three years of USDA production reports or Board assessment reports if USDA production reports are unavailable; (2) shifts and trends in quantities of watermelon produced, and (3) other relevant factors. As a result of the review, the Board may recommend to USDA that the districts be realigned.

Pursuant to section 1210.501, the seven current districts are as follows:

District 1—The State of Florida;

District 2—The States of Kentucky, North Carolina, South Carolina, Tennessee, Virginia and West Virginia;

District 3—The State of Georgia;

District 4—The States of Connecticut, Delaware, Illinois, Indiana, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont, Wisconsin, and Washington, DC;

District 5—The State of California;

District 6—The State of Texas;

District 7—The States of Alabama, Alaska, Arizona, Arkansas, Colorado, Hawaii, Idaho, Iowa, Kansas, Louisiana, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oklahoma, Oregon, South Dakota, Utah, Washington, and Wyoming.

The districts listed above were recommended by the Board in 2016 and established through rulemaking by USDA in 2017 (82 FR 44966).

In 2019, the Board's Executive Committee conducted a review of the U.S. watermelon production districts to determine whether realignment was necessary. The committee held teleconferences on August 14 and September 11, 2019, and reviewed production data for 2016, 2017 and 2018 from USDA's National Agricultural Statistics Service's (NASS) Vegetables Annual Summary for 2018 and Market News Reports. Due to changes in the geographical coverage of USDA's data collection on watermelon production, Board assessment data was used for the states for which USDA data was not available. To protect personally identifiable information (PII) of watermelon producers and handlers, the average of 2016–2018 assessment data was converted to a percentage of production. The combined data is shown in Table 1 below.

TABLE 1—STATE PRODUCTION BASED ON USDA AND BOARD ASSESSMENT DATA 2016–2018

State	Percent of 3-year average of U.S. production
Alabama	0.2
Arizona	2.9
Arkansas	0.8
California	13.8
Colorado	0.4
Delaware	2.8
Florida	17.9
Georgia	18.0
Hawaii	0.1
Illinois	1.8
Indiana	10.6
Kentucky	0.2
Louisiana	0.1
Maryland	1.9
Michigan	2.3
Mississippi	0.2
Missouri	4.3
Nebraska	0.2
New Mexico	0.6
New York	0.6
North Carolina	4.0
Ohio	0.1
Oklahoma	0.2
Oregon	1.0
South Carolina	1.8
Texas	11.8
Virginia	0.3
Washington	1.1

Upon review, the Board, at its October 26, 2019 meeting, recommended a reduction in the number of U.S. production districts from seven to five, resulting in a total of ten producer members and ten handler members. The proposed action recommended eliminating two districts, retaining two districts as drawn, and creating three new production districts as follows:

District 1—The State of Florida (no change);

District 2—The State of Georgia (formerly District 3).

District 3—The States of Alabama, Arkansas, Louisiana, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, and Texas.

District 4—The States of Connecticut, Delaware, Illinois, Indiana, Kentucky, Maryland, Massachusetts, Maine, Michigan, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont, Virginia, West Virginia, Wisconsin, and Washington, DC.

District 5—The States of Alaska, Arizona, California, Colorado, Hawaii, Idaho, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington, and Wyoming.

As shown in Table 2, each district will represent close to 20 percent of the total U.S. production, with a range of approximately 18 to 24.5 percent. USDA has reviewed NASS, Market News, and Board assessment data, and as shown in Table 2, determined that the production estimates are consistent with the Board's recommendation.

TABLE 2—PERCENT OF U.S. PRODUCTION BY DISTRICT [1]

District	Board data (%)	USDA analysis (%)	Difference (%)
1	17.8	18.2	+0.4
2	18.0	18.0	None
3	19.0	19.2	+0.2
4	20.6	20.7	+0.1
5	24.5	23.9	−0.6

Section 1210.501 will be revised accordingly.

Review of Imports

Section 1210.320(e) requires USDA to evaluate the average annual percentage of assessments paid by importers during the three-year period preceding the date of the evaluation and adjust, to the extent practicable, the number of importer representatives on the Board.

Table 4 below shows domestic and import assessment data for watermelons for the years 2016, 2017 and 2018. The data is from the Board's financial audits for 2016, 2017 [2] and 2018.

[1] Table values were rounded to the nearest percent.

[2] National Watermelon Promotion Board, Financial Statements and Supplementary Information, Years Ending March 31, 2016, 2017, and 2018, BDO USA, LLP.

TABLE 4—U.S. AND IMPORT ASSESSMENT DATA FOR 2016–2018

Year	Domestic (U.S.) assessments	Import assessments	Total
2016	$2,319,704	$1,172,834	$3,492,538
2017	2,347,522	1,049,875	3,397,397
2018	2,311,116	1,041,244	3,352,360
3-Year Average	2,326,114	1,087,984	3,414,098
Percent of Total	68 percent	32 percent	

Based on this data, the three-year average annual import assessments for watermelons for 2016–2018 was $1,087,984, approximately 32 percent of the Board's assessment income. To make the number of importers on the Board proportionate to the assessments paid as well as to the percentages of U.S. watermelon produced by the reduced number of production districts, the number of importers should decrease from twelve to nine members.

With this amendment, the new composition of board membership will be reflected in section 1210.502. According to the Board, this action will accurately reflect the distribution of the production and handling of watermelons, and the resulting reduced number of producer, handler, and importer seats will contribute to the effective administration of the program.

Final Regulatory Flexibility Act Analysis

In accordance with the Regulatory Flexibility Act (RFA) (5 U.S.C. 601–612), AMS is required to examine the economic impact of this rule on small entities. Accordingly, AMS has considered the economic impact of this action on such entities.

The purpose of the RFA is to fit regulatory actions to the scale of businesses subject to such actions so that small businesses will not be disproportionately burdened. The Small Business Administration defines, in 13 CFR part 121, small agricultural producers as those having annual receipts of no more than $1,000,000 and small agricultural service firms (handlers and importers) as those having annual receipts of no more than $30 million.

According to the Board, there are 505 producers, 140 handlers, and 252 importers who were required to pay assessments under the Plan in 2018. NASS data for the 2018 crop year estimated about 350.5 hundredweight (cwt.) of watermelons were produced per acre in the United States, and the 2018 grower price was $16.90 per cwt.[3] Thus, the value of watermelon production per acre in 2018 averaged about $5,923 (350.5 cwt. × $16.90). At that average valuation, a producer would have to farm over 169 acres to receive an annual income from watermelons of $1,000,000 ($1,000,000 divided by $5,923 per acre equals approximately 169 acres). Using 2017 USDA Census of Agriculture data, a maximum of 373 farms had watermelon acreage greater than or equal to 100 acres, and 13,147 out of a total of 13,520 farms producing watermelons reported less than 100 acres of watermelon on their farms.[4] Therefore, assuming watermelon producers operate no more than one farm, a majority of all U.S. watermelon farms would be classified as small businesses.

Also based on the Board's data, using a price of $0.169 per pound and the number of pounds handled annually, none of the watermelon handlers have receipts over the $30 million threshold.[5] [6] Therefore, all watermelon handlers will be considered small businesses. A handler would have to ship over 177 million pounds of watermelons to be considered large (177,514,793 × $0.169 f.o.b. equals approximately $30,000,000).

Based on 2018 Customs data, over 99 percent of watermelon importers shipped less than $30 million worth of watermelons that year. Based on the above-mentioned data the majority of watermelon producers, handlers and importers that will be affected by this rule will be classified as small entities.

Regarding the value of the commodity, based on 2018 NASS data, the value of the U.S. watermelon crop was about $656.6 million.[7] According to Customs data, the value of 2018 imports was about $312.4 million.

The rule revises sections 1210.321, 1210.403, 1210.501 and 1210.502 of the Plan to reduce the number of U.S. production districts from seven to five, thus eliminating two districts, retaining two districts as drawn, and creating three new districts. Accordingly, section 1210.320 requires the number of importer members to also decrease proportionately from 12 to 9 members, for a total of 30 Board members. The revisions are administrative in nature; therefore, there should be no economic impact on producers, handlers, or importers.

Under the program, the United States is currently divided into seven districts of comparable production volumes of watermelons, and each district is allocated two producer members and two handler members. Further, importer representation on the Board must be, to the extent practicable, proportionate to the percentage of assessments paid by importers, except there must be at least one importer on the Board.

Regarding the economic impact of the proposed rule on affected entities, neither the reduction in the number of production districts nor the reduction in Board membership imposes any additional costs on industry members. The recommended changes are necessary to improve the Board's ability to ensure both a quorum at Board meetings and a sufficient number of potential nominees. Further, the accompanying reduction of importer seats from twelve to nine provides for the equitable representation of producers, handlers and importers on the Board.

Regarding alternatives, the Board considered another scenario in realigning the districts. This scenario (Scenario 1) would have divided the U.S. into four production districts as follows:

District 1 would be comprised of the States of Florida, North Carolina, and South Carolina;

[3] Vegetables, 2018 Summary, March 2019, USDA, p. 10.; *https://downloads.usda.library.cornell.edu/usda-esmis/files/02870v86p/gm80j322z/5138jn50j/vegean19.pdf.*

[4] 2017 Census of Agriculture, April 11, 2019, USDA, National Agricultural Statistics Service, p. 39; *https://www.nass.usda.gov/Publications/AgCensus/2017/Full_Report/Volume_1,_Chapter_1_US/usv1.pdf.*

[5] Vegetables, 2018 Summary, March 2019, USDA, *https://downloads.usda.library.cornell.edu/usda-esmis/files/02870v86p/gm80j322z/5138jn50j/vegean19.pdf.*

[6] National Watermelon Promotion Board assessment records, 2016–2018.

[7] Vegetables, 2018 Summary, March 2019, USDA, p. 10.

District 2 would be comprised of the States of Connecticut, Delaware, Georgia, Maryland, Massachusetts, Maine, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Vermont, Virginia, West Virginia, and Washington, DC;

District 3 would be comprised of the States of Alabama, Arkansas, Illinois, Indiana, Kentucky, Louisiana, Mississippi, Ohio, Oklahoma, Tennessee, and Texas.

District 4 would be comprised of the States of Alaska, Arizona, California, Colorado, Hawaii, Idaho, Iowa, Kansas, Michigan, Minnesota, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington, Wisconsin, and Wyoming.

In accordance with the Plan, both scenarios preserve the composition of 2 producers and 2 handlers per district. Ultimately the Board recommended Scenario 2 at their October 26, 2019, retaining the State of Florida as District 1, changing the district designation for Georgia from District 3 to District 2, and creating new Districts 3, 4, and 5.

The changes to the size of the Board, number of production districts, and number of importer members are administrative in nature and have no economic impact on entities covered under the program. As some producers and handlers operate in multiple districts, they would be able to seek nomination for a district of their choice.

Reporting and Recordkeeping Requirements

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35), the Plan's information collection requirements have been previously approved by OMB under OMB control number 0581–0093. This rule does not result in a change to the information collection and recordkeeping requirements previously approved and does not impose additional reporting requirements or recordkeeping burden on domestic producers, handlers, or importers of watermelon.

As with all Federal research and promotion programs, reports and forms are periodically reviewed to reduce information requirements and duplication by industry and public-sector agencies. USDA has not identified any relevant Federal rules that duplicate, overlap, or conflict with this rule. AMS is committed to complying with the E-Government Act, to promote 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.

The Board met on October 26, 2019, and recommended realignment of the Board by reducing the number of production districts and proportionally reducing the number of importer seats on the Board from twelve to nine.

A proposed rule concerning this action was published in the **Federal Register** on April 27, 2020 (85 FR 23248). A 30-day comment period ending May 27, 2020, was provided to allow interested persons to submit comments.

Analysis of Comments

Eleven comments were received in response to the proposed rule. Of those eleven comments, ten supported the proposed realignment and reduction in production districts and the reduction of three importer seats. One comment expressed concerns with the proposal.

The comments that supported the proposed changes concur that the proposal accurately reflects changes in the volume of imports and the geographical distribution of watermelon production in the United States. Further, the consolidation of some districts also reflects consolidations throughout the watermelon industry and will make it easier for the Board to find qualified candidates to fill vacancies. Several commenters mentioned that as an added benefit, the reduction in Board membership will also reduce costs for Board meetings, thereby leaving more funds available for watermelon research and promotion activities.

One comment expressed concerns with the proposed rule. The commenter expressed concern that the justification for the Board's recommendation was ambiguous because the ''other relevant factors'' considered as part of the § 1210.320(c) review were not formally defined or explained in the proposal. At its October 26, 2019 Board meeting, which was open to the public, the Board discussed three relevant factors in addition to the production and import data presented in the proposal. First, Board members shared their observations that consolidation in the watermelon industry over the past decade had substantially reduced the number of eligible producers and handlers in the production districts as they are currently drawn. A related issue also discussed was the fact that despite concerted outreach efforts, obtaining enough candidates and nominees to be considered for appointment to the Board had become extremely difficult in recent years. Finally, several members observed that attendance at Board meetings has declined to the point where it is consistently difficult to ensure a quorum.

No changes have been made to the proposed rule based on the comments received.

After consideration of all relevant matters presented, including the information and recommendation submitted by the Board, the comments received, and other relevant information, it is hereby found that this rule, as hereinafter set forth, is consistent with and would effectuate the purposes of the Act.

List of Subjects in 7 CFR Part 1210

Administrative practice and procedure, Advertising, Consumer information, Marketing agreements, Reporting and recordkeeping requirements, Watermelon promotion.

For the reasons set forth in the preamble, 7 CFR part 1210 is amended as follows:

PART 1210—WATERMELON RESEARCH AND PROMOTION PLAN

■ 1. The authority citation for 7 CFR part 1210 continues to read as follows:

Authority: 7 U.S.C. 4901–4916 and 7 U.S.C. 7401.

Subpart C—Rules and Regulations

■ 2. In § 1210.321, revise paragraph (f)(1) to read as follows:

§ 1210.321 Realignment of districts.

* * * * *

(f) * * *

(1) No State in a multi-State district shall have more than three producer and handler representatives concurrently on the Board.

* * * * *

■ 3. In § 1210.403, revise paragraph (c) to read as follows:

§ 1210.403 Voting Procedures.

* * * * *

(c) In multi-State districts, the convention chairperson will direct the eligible producer voters and handler voters from each State to caucus separately for the purpose of electing a State spokesperson for each group. Election of each State spokesperson shall be by simple majority of all individual voters in attendance. In lieu of written ballots, a State spokesperson may be elected by voice vote or a show of hands. The role of the State spokesperson is to coordinate State voting and to cast all State votes.

* * * * *

■ 4. Revise § 1210.501 to read as follows:

§ 1210.501 Realignment of districts.

In accordance with § 1210.320(c) of the Plan, the districts shall be as follows:

(a) *District 1*—The State of Florida.

(b) *District 2*—The State of Georgia.

(c) *District 3*—The States of Alabama, Arkansas, Louisiana, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, and Texas.

(d) *District 4*—The States of Connecticut, Delaware, Illinois, Indiana, Kentucky, Maryland, Massachusetts, Maine, Michigan, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont, Virginia, West Virginia, Wisconsin, and Washington, DC.

(g) *District 5*—The States of Alaska, Arizona, California, Colorado, Hawaii, Idaho, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington, and Wyoming.

■ 5. Revise § 1210.502 to read as follows:

§ 1210.502 Board members.

The Board consists of 10 producers, 10 handlers, nine importers, and one public member appointed by the Secretary.

Bruce Summers,

Administrator, Agricultural Marketing Service.

[FR Doc. 2020–17581 Filed 9–11–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF ENERGY

10 CFR Parts 429 and 430

[EERE–2017–BT–TP–0005]

RIN 1904–AD67

Energy Conservation Program: Test Procedure for Fluorescent Lamp Ballasts

AGENCY: Office of Energy Efficiency and Renewable Energy, Department of Energy.

ACTION: Final rule.

SUMMARY: On March 18, 2019, the U.S. Department of Energy (''DOE'') published a notice of proposed rulemaking (''NOPR'') to amend the test procedure for fluorescent lamp ballasts. That proposed rulemaking serves as the basis for the final rule. Specifically, in this final rule, DOE updates references to industry standards; clarifies the selection of reference lamps; removes extraneous requirements in the stabilization procedure; provides a second stabilization option for measuring ballast luminous efficiency; and revises the test procedure for measuring standby mode energy consumption.

DATES: The effective date of this rule is October 14, 2020. The final rule changes will be mandatory for product testing starting March 15, 2021. The incorporation by reference of certain publications listed in this rulemaking is approved by the Director of the Federal Register on October 14, 2020. The incorporation by reference of certain other publications listed in this rulemaking was approved by the Director of the Federal Register on June 3, 2011.

ADDRESSES: The docket, which includes **Federal Register** notices, comments, and other supporting documents/materials, is available for review at *http://www.regulations.gov.* All documents in the docket are listed in the *http://www.regulations.gov* index. However, some documents listed in the index, such as those containing information that is exempt from public disclosure, may not be publicly available.

A link to the docket web page can be found at *https://www.regulations.gov/docket?D=EERE-2017-BT-TP-0005.* The docket web page contains instructions on how to access all documents, including public comments, in the docket.

For further information on how to review the docket contact the Appliance and Equipment Standards Program staff at (202) 287–1445 or by email: *ApplianceStandardsQuestions@ee.doe.gov.*

FOR FURTHER INFORMATION CONTACT: Ms. Lucy deButts, U.S. Department of Energy, Office of Energy Efficiency and Renewable Energy, Building Technologies Office, EE–5B, 1000 Independence Avenue SW, Washington, DC 20585–0121. Telephone: (202) 287–1604. Email: *ApplianceStandardsQuestions@ee.doe.gov.*

Ms. Sarah Butler, U.S. Department of Energy, Office of the General Counsel, GC–33, 1000 Independence Avenue SW, Washington, DC 20585–0121. Telephone: (202) 586–1777. Email: *Sarah.Butler@hq.doe.gov.*

SUPPLEMENTARY INFORMATION: DOE maintains previously approved incorporation by references and incorporates by reference the following industry standards into 10 CFR part 430:

ANSI C78.81, (''ANSI C78.81–2016''), American National Standard for Electric Lamps—Double-Capped Fluorescent Lamps—Dimensional and Electrical Characteristics, approved June 29, 2016.

ANSI C78.375A–2014, (''ANSI C78.375A''), American National Standard for Electric Lamps—Fluorescent Lamps—Guide for Electrical Measures, approved August 28, 2014.

ANSI/NEMA C78.901–2016, (''ANSI C78.901–2016''), American National Standard for Electric Lamps—Single-Based Fluorescent Lamps—Dimensional and Electrical Characteristics, ANSI approved August 23, 2016.

ANSI C82.1–2004 (R2008, R2015), (''ANSI C82.1''), American National Standard for Lamp Ballasts—Line Frequency Fluorescent Lamp Ballast, approved November, 20, 2015.

ANSI C82.2–2002 (R2007, R2016), (''ANSI C82.2''), American National Standard for Lamp Ballasts—Method of Measurement of Fluorescent Lamp Ballasts, approved July 12, 2016.

ANSI C82.3–2016, (''ANSI C82.3''), American National Standard for Lamp Ballasts—Reference Ballasts for Fluorescent Lamps, approved April 8, 2016.

ANSI/NEMA C82.11–2017, (''ANSI C82.11''), American National Standard for Lamp Ballasts—High-frequency Fluorescent Lamp Ballasts, approved January 23, 2017.

ANSI C82.13–2002, (''ANSI C82.13''), American National Standard for Lamp Ballasts—Definitions for Fluorescent Lamps and Ballasts, approved July 23, 2002.

ANSI C82.77–2002, (''ANSI C82.77''), Harmonic Emission Limits—Related Power Quality Requirements for Lighting Equipment, approved January 17, 2002.

Copies of ANSI C78.81–2016, ANSI C78.375A, ANSI C78.901–2016, ANSI C82.1, ANSI C82.2, ANSI C82.3, ANSI C82.11, ANSI C82.13, and ANSI C82.77, are available at *http://www.ansi.org* or *http://www.nema.org.*

International Electrotechnical Commission (''IEC'') Standard 60081, (''IEC 60081''), Double-capped fluorescent lamps—Performance specifications (Amendment 6, Edition 5.0, August 2017).

IEC 62301:2011, (''IEC 62301''), Household electrical appliances—Measurement of standby power, (Edition 2.0, 2011–01).

Copies of IEC 60081 and IEC 62301 are available on IEC's website at *https://webstore.iec.ch/home.*

For a further discussion of these standards, see section IV.O.

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I. Authority and Background

Fluorescent lamp ballasts are included in the list of ''covered products'' for which DOE is authorized to establish and amend energy conservation standards and test procedures. (42 U.S.C. 6292(a)(13)) DOE's energy conservation standards and test procedures for fluorescent lamp ballasts are currently prescribed in the Code of Federal Regulations (''CFR'') at 10 CFR 430.32(m) and 10 CFR 430.23(q), respectively. The following sections discuss DOE's authority to establish test procedures for fluorescent lamp ballasts and relevant background information regarding DOE's consideration of test procedures for these products.

A. Authority

The Energy Policy and Conservation Act, as amended (''EPCA''),[1] authorizes DOE to regulate the energy efficiency of a number of consumer products and certain industrial equipment. (42 U.S.C. 6291–6317) Title III, Part B[2] of EPCA established the Energy Conservation Program for Consumer Products Other Than Automobiles, which sets forth a variety of provisions designed to improve energy efficiency. These consumer products include fluorescent lamp ballasts, the subject of this document. (42 U.S.C. 6292(a)(13))

The energy conservation program under EPCA consists essentially of four parts: (1) Testing, (2) labeling, (3) Federal energy conservation standards, and (4) certification and enforcement procedures. Relevant provisions of EPCA specifically include definitions (42 U.S.C. 6291), test procedures (42 U.S.C. 6293), labeling provisions (42 U.S.C. 6294), energy conservation standards (42 U.S.C. 6295), and the authority to require information and reports from manufacturers. (42 U.S.C. 6296)

The testing requirements consist of test procedures that manufacturers of covered products must use as the basis for (1) certifying to DOE that their products comply with the applicable energy conservation standards adopted under EPCA (42 U.S.C. 6295(s)), and (2) making representations about the efficiency of those products (42 U.S.C. 6293(c)). Similarly, DOE must use these test procedures to determine whether the products comply with any relevant standards promulgated under EPCA. (42 U.S.C. 6295(s))

Federal energy efficiency requirements for covered products established under EPCA generally supersede State laws and regulations concerning energy conservation testing, labeling, and standards. (42 U.S.C. 6297) DOE may, however, grant waivers of Federal preemption for particular State laws or regulations, in accordance with the procedures and other provisions of EPCA. (42 U.S.C. 6297(d))

Under 42 U.S.C. 6293, EPCA sets forth the criteria and procedures DOE must follow when prescribing or amending test procedures for covered products. EPCA provides that any test procedures prescribed or amended under this section shall be reasonably designed to produce test results which measure energy efficiency, energy use or estimated annual operating cost of a covered product during a representative average use cycle or period of use and shall not be unduly burdensome to conduct. (42 U.S.C. 6293(b)(3))

In addition, EPCA requires that DOE amend its test procedures for all covered products to integrate measures of standby mode and off mode energy consumption into the overall energy efficiency, energy consumption, or other energy descriptor, unless the current test procedure already incorporates the standby mode and off mode energy consumption, or if such integration is technically infeasible. (42 U.S.C. 6295(gg)(2)(A)) If an integrated test procedure is technically infeasible, DOE must prescribe separate standby mode and off mode energy use test procedures for the covered product, if a separate test is technically feasible. (*Id.*) Any such amendment must consider the most current versions of the International Electrotechnical Commission (''IEC'') Standard 62301 (''IEC 62301'')[3] and IEC Standard 62087[4] as applicable. (42 U.S.C. 6295(gg)(2)(A))

If DOE determines that a test procedure amendment is warranted, it must publish a proposed test procedure and offer the public an opportunity to present oral and written comments on it. (42 U.S.C. 6293(b)(2))

EPCA also requires that, at least once every 7 years, DOE evaluate test procedures for each type of covered product, including fluorescent lamp ballasts, to determine whether amended test procedures would more accurately or fully comply with the requirements for the test procedures to not be unduly burdensome to conduct and be reasonably designed to produce test results that reflect energy efficiency, energy use, and estimated operating costs during a representative average use cycle or period of use. (42 U.S.C. 6293(b)(1)(A)) If the Secretary determines, on his own behalf or in response to a petition by any interested person, that a test procedure should be prescribed or amended, the Secretary shall promptly publish in the **Federal Register** proposed test procedures and afford interested persons an opportunity to present oral and written data, views, and arguments with respect to such procedures. The comment period on a proposed rule to amend a test procedure shall be at least 60 days and may not exceed 270 days. In prescribing or amending a test procedure, the Secretary shall take into account such information as the Secretary determines relevant to such procedure, including technological developments relating to

[1] All references to EPCA in this document refer to the statute as amended through America's Water Infrastructure Act of 2018, Public Law 115–270 (October 23, 2018).

[2] For editorial reasons, upon codification in the U.S. Code, Part B was redesignated Part A.

[3] IEC Standard 62301, *Household electrical appliances—Measurement of standby power* (Edition 2.0, 2011–01).

[4] IEC Standard 62087, *Methods of measurement for the power consumption of audio, video, and related equipment* (Edition 3.0, 2011–04).

energy use or energy efficiency of the type (or class) of covered products involved. (42 U.S.C. 6293(b)(2)) If DOE determines that test procedure revisions are not appropriate, DOE must publish its determination not to amend the test procedures. DOE is publishing this final rule in satisfaction of the 7-year review requirement specified in EPCA. (42 U.S.C. 6293(b)(1)(A))

DOE's test procedure for fluorescent lamp ballasts appears at 10 CFR part 430, subpart B, appendix Q (''appendix Q''). DOE's energy conservation standards for fluorescent lamp ballasts can be found at 10 CFR 430.32(m) and require a minimum power factor and minimum ballast luminous efficiency (''BLE''). In this final rule, DOE updates references to industry standards; clarifies the selection of reference lamps; provides a second stabilization option for measuring ballast luminous efficiency; and revises the test procedure for measuring standby mode energy consumption.

B. Background

DOE published a final rule establishing an active mode test procedure for fluorescent lamp ballasts on April 24, 1991. 56 FR 18677. DOE last completed a full review of the active mode test procedure for fluorescent lamp ballasts on May 4, 2011. 76 FR 25211. Some of the key amendments in that test procedure final rule included updates to industry standards, adopting BLE as the metric for measuring energy efficiency of fluorescent lamp ballasts, and expanding the test procedure to apply to additional products.

DOE published a final rule establishing a standby mode energy consumption test procedure for fluorescent lamp ballasts on October 22, 2009. 74 FR 54445. DOE determined that, according to EPCA's definition of standby mode,[5] fluorescent lamp ballasts capable of standby mode operation are designed to operate in, or function as, a lighting control system where auxiliary control devices send signals to the ballast; and at zero light output, the ballast is standing by, connected to a main power source without being disconnected by an on-off switch or other type of relay. Further, DOE determined that it is not possible for fluorescent lamp ballasts to meet EPCA's definition of ''off mode,''[6] because there is no condition in which the ballast is connected to the main power source and is not in a mode already accounted for in either active mode or standby mode. 74 FR 54445, 54448.

DOE published final rules establishing and amending energy conservation standards for fluorescent lamp ballasts on September 19, 2000, and November 14, 2011, respectively. 65 FR 56740; 76 FR 70547. DOE also published final rules on February 4, 2015, June 5, 2015, and April 29, 2016, to correct and clarify certain requirements and specifications in the CFR relating to energy conservation standards and test procedures. 80 FR 5896; 80 FR 31971; 81 FR 25595. On June 23, 2015, DOE initiated a rulemaking to review energy conservation standards for fluorescent lamp ballasts by publishing a **Federal Register** notice announcing a public meeting and availability of the framework document (''June 2015 framework document''). 80 FR 35886. On October 22, 2019, DOE published a notice of proposed determination (''NOPD'') initially determining that energy conservation standards for fluorescent lamp ballasts do not need to be amended. 84 FR 56540 (''October 2019 NOPD''). DOE held a webinar open to the public on October 30, 2019, during which it described the analyses and results from the October 2019 NOPD and requested comments.[7]

On March 18, 2019, DOE published in the **Federal Register** a NOPR proposing amendments to the fluorescent lamp ballast (''FLB'') test procedure. 84 FR 9910 (''March 2019 NOPR''). This document addresses information and comments received in response to the March 2019 NOPR and details the amendments to the test procedure adopted in this final rule.

DOE received six written comments in response to the March 2019 NOPR from the interested parties listed in Table I.1 of this document.

TABLE I.1—WRITTEN COMMENTS RECEIVED IN RESPONSE TO MARCH 2019 NOPR

Organization(s)	Reference in this NOPR	Organization type
Appliance Standards Awareness Project, American Council for an Energy-Efficient Economy.	ASAP/ACEEE	Efficiency Organizations.
National Electrical Manufacturers Association	NEMA	Trade Association.
Lutron Electronics Co	Lutron	Manufacturer.
Signify North America Corporation	Signify	Manufacturer.
California Energy Commission	CEC	State Commission.
Pacific Gas and Electric Company, San Diego Gas and Electric, and Southern California Edison; collectively California Investor Owned Utilities.	CA IOUs	Utilities.

II. Synopsis of the Final Rule

In this final rule, DOE amends 10 CFR 430.3, 10 CFR 430.23(q), and appendix Q as follows: (1) Updates references to industry standards; (2) clarifies the selection of reference lamps; (3) removes extraneous requirements in the stabilization procedure; (4) provides a second stabilization option for measuring BLE; and (5) revises the test procedure for measuring standby mode energy consumption.

The amendments adopted for appendix Q are summarized in Table II.1 compared to the current test procedure as well as the reason for the adopted change.

[5] EPCA defines ''standby mode'' as the condition in which an energy-using product—(1) is connected to a main power source; and (2) offers 1 or more of the following user-oriented or protective functions: (i) To facilitate the activation or deactivation of other functions (including active mode) by remote switch (including remote control), internal sensor, or timer. (ii) Continuous functions, including information or status displays (including clocks) or sensor-based functions. (42 U.S.C. 6295(gg)(1)(A)(iii))

[6] EPCA defines ''off mode'' as ''the condition in which an energy-using product—(I) is connected to a main power source; and (II) is not providing any standby or active mode function.'' (42 U.S.C. 6295(gg)(1)(A)(ii))

[7] A transcript of the public webinar and supporting documents are available in the docket for this proposed determination at: *https://www.regulations.gov/docket?D=EERE-2015-BT-STD-0006.*

TABLE II.1—SUMMARY OF CHANGES IN THE AMENDED TEST PROCEDURE

Current DOE test procedure	Amended test procedure	Attribution
References the 2002 version of ANSI C82.11 for testing high frequency ballasts.	Adds checks on inrush current and references lamp datasheets in ANSI C78.81 and ANSI C78.901 for appropriate maximum glow current.	Industry update to ANSI C82.11.
References lamp datasheets in ANSI C78.81 to specify the appropriate reference lamp to use when testing a particular ballast.	The 2016 version of ANSI C78.81 updates the high frequency characteristics of three lamps currently referenced in Table A.	Industry update to ANSI C78.81.
References lamp datasheets in IEC 60081 Amendment 4 to specify the appropriate reference lamp to use when testing a particular ballast.	Amendment 6 of IEC 60081 updates the high frequency characteristics of two lamps currently referenced in Table A.	Industry update to IEC 60081.
Does not provide detail to determine which lamp to use for testing when ballasts can operate lamps of more than one base type.	Adds direction for how to select a reference lamp to use for testing fluorescent lamp ballasts designed and marketed to operate lamps of multiple base types.	Improve representativeness of test results.
Measures lamp arc voltage, current, and power once per second during stabilization.	Measures lamp arc voltage, current, and power once per minute during stabilization.	Reduce test burden while maintaining representative results.
Operates ballast for no longer than one hour until stable operating conditions are met.	No maximum operating time until stable operating conditions are met.	Reduce test burden while maintaining representative results.
Has one method of stabilization where lamp arc voltage, current, and power are measured once per second until the difference between the maximum and minimum values do not exceed one percent over a four minute moving window.	Allows a second stabilization option where an oven is used to heat the ballasts prior to testing and lamp arc voltage, current, and power are measured once per minute.	Reduce test burden while maintaining representative results.
Measures standby mode power by referencing ANSI C82.2.	References IEC 62301 to measure standby mode power.	Improve the repeatability and reproducibility of test results.
Ballast connects to reference lamp while measuring standby mode power.	Reference lamps are not required when measuring standby mode power.	Reduce test burden while maintaining representative results.
Standby power test conditions are based on conditions defined in ANSI C82.2, which do not include instructions specifying input voltage.	Standby power test conditions are based on conditions defined in appendix Q for the active mode measurement, which include specifications for which input voltage to operate ballasts designed and marketed to operate at multiple input voltages.	Improve representativeness, repeatability, and reproducibility of test results.

DOE is also amending the reporting requirements under 10 CFR 429.26 to require reporting average total lamp arc power, a value that is already determined in appendix Q; specify rounding requirements for average total lamp arc power; and remove references to values no longer required.

DOE has determined that the amendments described in section III of this document and adopted in this final rule will not alter the measured efficiency of fluorescent lamp ballasts, and that the test procedure will not be unduly burdensome to conduct. Discussion of DOE's actions are addressed in detail in section III of this document.

The effective date for the amended test procedure adopted in this final rule is October 14, 2020. Representations of energy use or energy efficiency must be based on testing in accordance with the amended test procedures beginning March 15, 2021.

III. Discussion

A. Scope of Applicability

This rulemaking applies to fluorescent lamp ballasts, which are devices that can start and operate fluorescent lamps by providing a starting voltage and current and limiting the current during normal operation. 10 CFR 430.2. DOE defines a fluorescent lamp as a lamp of certain shapes, lengths, bases, and wattages [8] that is a low pressure mercury electric-discharge source in which a fluorescing coating transforms some of the ultraviolet energy generated by the mercury discharge into light. 10 CFR 430.2.

DOE received comments regarding potential amendments to FLB energy conservation standards. NEMA commented that the market for fluorescent lamps and fluorescent lamp ballasts (particularly, dimming ballasts) is decreasing substantially due to the transition to solid-state lighting (''SSL''). (NEMA, No. 3 at p. 2) [9] NEMA stated that manufacturers are not currently investing, nor are expected to invest, material resources in fluorescent lamp ballasts. *Id.* NEMA added there have been no technological changes since the adoption of the current FLB standards and amending these standards will not result in new investment but rather discontinuance of products. *Id.* ASAP/ACEEE stated it could take many years for existing fluorescent systems to transition to SSL, and fluorescent lighting is still competitive on a lifecycle cost basis. (ASAP/ACEEE, No. 8 at p. 1)

Lutron asserted that amended FLB standards are not technologically feasible due to lack of any technological breakthrough in FLB technology and are not economically justified due to the FLB market decline. (Lutron, No. 6 at p. 2) Lutron added that amended FLB standards are unlikely to meet the energy savings threshold envisioned in the Process Rule. *Id.*

As discussed, DOE issued the October 2019 NOPD in which it initially determined that energy conservation standards for fluorescent lamp ballasts do not need to be amended. 84 FR 56540. DOE will address potential

[8] See definition of ''fluorescent lamps'' in 10 CFR 430.2 for the specific lamps defined as fluorescent lamps.

[9] A notation in the form ''NEMA, No. 3 at p. 2'' identifies a written comment: (1) Made by NEMA; (2) recorded in document number 3 that, unless otherwise specified, is filed in the docket of this test procedure rulemaking (Docket No. EERE–2017–BT–TP–0005–0003) and available for review at *http://www.regulations.gov;* and (3) which appears on page 2 of document number 3.

amendments to the energy conservation standards under that separate review.

Lutron stated DOE should adopt a ''No-Rule Rule'' and not amend FLB test procedures for the following reasons: (1) No technological breakthroughs or investments in fluorescent lamp ballasts since the last rulemaking, (2) decline in FLB sales due to adoption of light emitting diode (''LED'') technology, (3) ballasts are highly efficient, and dimming ballasts already save significant energy over standard non-dimming ballasts, and (4) updating test procedures may result in a significant regulatory burden for manufacturers without achieving energy savings. (Lutron, No. 6 at p. 2)

NEMA stated that, while it was appropriate to update the FLB test procedure as proposed, compliance to the changes should not be effective until amendments to FLB standards are justified in accordance with EPCA. NEMA asserted that some manufacturers may incur higher test cost burdens which should only be imposed if amended FLB standards are justified. (NEMA, No. 3 at pp. 2–3) Lutron stated that, if a ''No-Rule-Rule'' is not possible, it agreed with NEMA's suggestion of aligning the compliance date of amended FLB test procedures and amended FLB standards. (Lutron, No. 6 at pp. 2–3)

In the March 2019 NOPR, DOE preliminarily determined that the proposed amendments to its FLB test procedure would not change measured values; and therefore, would not require manufacturers to retest fluorescent lamp ballasts previously tested and certified under the previous test procedure. The amendments being adopted in this final rule further align the DOE test procedure with industry standards and best practices and clarify existing test methods. As described, DOE has determined that the amendments adopted in this final rule will not alter the measured efficiency of fluorescent lamp ballasts; hence, there is no need to delay the compliance date of the amendments. Additionally, DOE has determined the amendments being adopted in this final rule do not add regulatory burden (see section III.I of this document).

ASAP/ACEEE commented that DOE should address the issue resulting from the statutory exclusion from the definition of general service fluorescent lamps (''GSFLs'') those lamps with a color rendering index (''CRI'') of 87 or greater (''high CRI''). They stated that the exclusion has allowed large numbers of inexpensive T12 [10] linear fluorescent lamps with high CRI to be sold and that these lamps are significantly less efficient than standards-compliant GSFLs. ASAP/ACEEE stated that the sale of high CRI T12 lamps has allowed a continued market for T12 ballasts, and thereby inefficient T12 fluorescent lighting systems.[11] (ASAP/ACEEE, No. 8 at p. 3)

As noted, this rulemaking addresses the test procedure for fluorescent lamp ballasts and does not address GSFLs. The amendments to the test procedure adopted in this final rule are updates to industry standard references and clarifications to the test methods and do not impact the sale of fluorescent lamp ballasts or associated products such as fluorescent lamps.

B. Updates to Industry Standards

The FLB test procedure references several industry standards. Industry periodically updates its testing standards to account for changes in technology and/or developments in test methodology and/or test instruments. In the March 2019 NOPR, DOE identified updated versions of the referenced industry standards incorporated by reference for appendix Q as shown in Table III.1 of this document. 84 FR 9910, 9913.

TABLE III.1—INDUSTRY STANDARDS REFERENCED IN APPENDIX Q WITH UPDATED VERSIONS ADOPTED IN FINAL RULE

Industry standard currently referenced in Appendix Q	Updated versions adopted in this Final Rule *
ANSI C82.11 [12] version 2002 (sections 2.1 and 2.4.1 of appendix Q)	ANSI C82.11 [13] version 2017.
ANSI C82.1 [14] version 2004 (sections 2.1, 2.3.1, and 2.4.1 of appendix Q).	ANSI C82.1 [15] version 2015.
ANSI C82.2 [16] version 2002 (sections 2.1, 2.2.1, 2.2.2, 2.2.3, 2.4.1, 2.4.3, 2.5.1.6, 2.5.1.7, 2.5.1.8, 3.2.1, 3.3.1, and 3.3.3 of appendix Q).	ANSI C82.2 [17] version 2016.
ANSI C82.3 [18] version 2002 (section 2.4.1 of appendix Q)	ANSI C82.3 [19] version 2016.
ANSI C78.375 [20] version 1997 (section 2.4.2 of appendix Q)	ANSI C78.375A [21] version 2014.
ANSI C78.901 [22] version 2005 (Table A of appendix Q)	ANSI C78.901 [23] version 2016.
ANSI C78.81 [24] version 2010 (sections 1.6, 1.7, 1.8, 2.1, 2.3.1, 2.4.1, and Table A of appendix Q).	ANSI C78.81 [25] version 2016.
IEC 60081 Amendment 4, Edition 5, 2010 [26] (Table A of appendix Q)	IEC 60081 Amendment 6, Edition 5, 2017. [27]

* Note: Additionally, this final rule incorporates by reference ANSI C82.77–2002 and IEC 62301 Edition 2.0 in appendix Q.

In the March 2019 NOPR, DOE compared updated and current versions

[10] T indicates the tubular shape of the lamp and the 12 is the diameter in eighths of an inch (*i.e.,* 12/8 inches).

[11] DOE's findings in previous rulemakings of GSFL energy conservation standards have shown that T8 lamps have a higher lamp efficacy (lumens per watt) than comparable T12 lamps. See documents from previous rulemaking at *https://www.regulations.gov/docket?D=EERE-2011-BT-STD-0006.*

[12] ANSI Standard C82.11, *American National Standard For Lamp Ballasts—High-frequency Fluorescent Lamp Ballasts—Supplements* (approved January 17, 2002).

[13] ANSI Standard C82.11, *American National Standard For Lamp Ballasts—High-frequency Fluorescent Lamp Ballasts* (approved January 23, 2017).

[14] ANSI Standard C82.1, *American National Standard For Lamp Ballasts—Line Frequency Fluorescent Lamp Ballast* (approved November, 19, 2004).

[15] ANSI Standard C82.1, *American National Standard For Lamp Ballasts—Line Frequency Fluorescent Lamp Ballast* (approved November, 20, 2015).

[16] ANSI Standard C82.2, *American National Standard for Lamp Ballasts—Method of Measurement of Fluorescent Lamp Ballasts* (approved June 6, 2002).

[17] ANSI Standard C82.2, *American National Standard for Lamp Ballasts—Method of Measurement of Fluorescent Lamp Ballasts* (approved July 12, 2016).

[18] ANSI Standard C82.3, *American National Standard for Lamp Ballasts—Reference Ballasts for Fluorescent Lamps* (approved September 4, 2002).

[19] ANSI Standard C82.3, *American National Standard for Lamp Ballasts—Reference Ballasts for Fluorescent Lamps* (approved April 8, 2016).

[20] ANSI Standard C78.375, *American National Standard For Fluorescent Lamps—Guide for Electrical Measures* (approved September, 25, 1997).

[21] ANSI Standard C78.375A, *American National Standard For Fluorescent Lamps—Guide for Electrical Measures* (approved August, 28, 2014).

Continued

to determine, as directed by EPCA, whether incorporating by reference the latest industry standards would alter measured energy efficiency. (42 U.S.C. 6293(e)(1)) For ANSI C82.2, DOE identified no substantial changes in the 2016 version compared to the 2002 version. For ANSI C82.1, DOE identified no substantial changes in the 2015 version compared to the 2004 version. For ANSI C78.375A, DOE identified no changes in the 2014 version compared to the 1997 version in the ambient conditions or electrical instruments instructions, for which the industry standard is referenced. 84 FR 9910, 9914–9916.

For ANSI C82.11, DOE identified several key changes in the 2017 version compared to the 2002 version. For ANSI C82.3, DOE identified several key changes in the 2016 version compared to the 2002 version. In the March 2019 NOPR DOE tentatively determined these changes would not result in changes to measured values of BLE because the differences do not result in substantive changes to test setup or methodology. 84 FR 9910, 9916.

ANSI C78.81, ANSI C78.901, and IEC 60081 consist of lamp datasheets referenced by Table A of the DOE FLB test procedure to specify the appropriate reference lamp to use when testing a particular ballast. In the March 2019 NOPR, DOE tentatively determined changes to the values of reference lamp characteristics in the latest 2016 versions of ANSI C78.81 and ANSI C 78.901 and IEC 60081 Amendment 6 are within testing tolerances and therefore, will have minimal impact on current requirements. However, the 2016 versions of ANSI C78.81 and ANSI C78.901 remove the low frequency specifications from lamp datasheets for the 32 W 4-foot medium bipin T8 lamp, 59 W 8-foot single pin T8 lamp, and 32 W 2-foot U-shaped medium bipin T8 lamp. Low frequency lamp characteristics and reference ballast characteristics are necessary to determine the appropriate reference lamp for testing low frequency ballasts. In the March 2019 NOPR, DOE proposed adding the low frequency specifications absent in the latest versions of the industry standards directly in appendix Q to ensure measured values are not impacted. 84 FR 9910, 9916–9917.

NEMA supported DOE's proposal to incorporate up-to-date industry standards. (NEMA, No. 3 at p. 3) ASAP/ACEEE also supported the updates if they improve the accuracy of the test procedures, avoid biasing the results, and provide representative results. (ASAP/ACEEE, No. 8 at p. 2) ASAP/ACEEE added that they were not aware of any such problems with the updates proposed. *Id.*

Consistent with its assessment in the March 2019 NOPR, DOE has determined that, because updates to industry standard references do not involve substantive changes to the test setup and methodology, they would not affect measured values. DOE has not identified any potential for bias or non-representative results under these updates as proposed. DOE has determined that incorporation by reference of the latest versions of industry standards will better align DOE's test procedure with updates to test methods that industry considers to be improvements to previous methods and also increase the clarity of DOE test methods. Hence, in this final rule DOE incorporates by reference for appendix Q the industry standards ANSI C78.81–2016, ANSI C78.375A–2014, ANSI C78.901–2016, ANSI C82.1–2004 (R2008, R2015), ANSI C82.2–2002 (R2007, R2016) (referred to as ANSI C82.2–2016 in this rulemaking), ANSI C82.3–2016, ANSI C82.11–2017, ANSI C82.77 and IEC 60081 Amendment 6 (see Table III.1).

Additionally, DOE is ensuring that the necessary low frequency specifications no longer in ANSI C78.81–2016 or ANSI C78.901–2016 remain available in appendix Q. Hence, in this final rule, for the 32 W 4-foot medium bipin T8 lamp, 59 W 8-foot single pin T8 lamp, and 32 W 2-foot U-shaped medium bipin T8 lamp, DOE is specifying directly in new section 2.3.3 of appendix Q the following low frequency specifications: (1) The low frequency lamp characteristics (*i.e.,* arc wattage, approximate cathode wattage, total wattage, voltage, and current), (2) reference ballast characteristics (*i.e.,* rated input voltage, reference current, impedance) and (3) cathode heating requirements for rapid start circuits. These specifications are the same as those in the earlier versions of the standards, ANSI C78.81–2010 and ANSI C78.901–2005.

In the March 2019 NOPR, DOE also proposed to incorporate by reference for appendix Q the following industry standards not already incorporated: (1) ANSI C82.77–2002 [28] because this standard is explicitly referenced by ANSI C82.11–2017, which DOE proposed to incorporate by reference; and (2) IEC 62301 [29] because it provides specific instructions for standby mode measurements. 84 FR 9910, 9914–9917.

Signify suggested that DOE reference the 2014 version of ANSI C82.77 rather than the 2002 version and noted that ANSI is currently working on an update, with expected publication in 2019. Signify specified that the two major changes in the 2014 version were to describe harmonic current limits for LED lighting and the displacement and harmonic factor optional power quality metric. (Signify, No. 7 at p. 1)

For testing high frequency ballasts, DOE's test procedure references the 2002 version of ANSI C82.11, which DOE is updating to the 2017 version in this final rule. While ANSI C82.11–2002 provides the limits for harmonic distortion of input currents, ANSI C82.11–2017 references ANSI C82.77–2002 for these limit specifications. The harmonic distortion input current limits in ANSI C82.77–2002 are the same as those specified in ANSI C82.11–2002. Because the update to ANSI C82.11 references the 2002 version of ANSI C82.77, DOE proposed to incorporate by reference ANSI C82.77–2002 into appendix Q. 84 FR 9910, 9915. Additionally, in its normative references section, ANSI C82.11–2017 states that at the time of publication the editions indicated are valid and lists the 2002 version of ANSI C82.77. While the section also encourages the possibility of applying the most recent editions, at the time of publication of ANSI C82.11–2017, the 2014 version of ANSI C82.77 was available but not referenced by the standard. The harmonic distortion input current limits for modular office furniture, which includes fluorescent lamp sources, is 155 percent in the 2014 version compared to 32 percent in the 2002 version. DOE notes that the key changes in the 2014 version of ANSI C82.77 noted by stakeholders are not

[22] ANSI Standard C78.901, *American National Standards for Electric Lamps—Single-Based Fluorescent Lamps—Dimensional and Electrical Characteristics* (approved March 23, 2005).

[23] ANSI Standard C78.901, *American National Standards for Electric Lamps—Single-Based Fluorescent Lamps—Dimensional and Electrical Characteristics* (approved August 23, 2016).

[24] ANSI Standard C78.81, *American National Standard For Electric Lamps—Double-Capped Fluorescent Lamps— Dimensional and Electrical Characteristics* (approved January, 14, 2010).

[25] ANSI Standard C78.81, *American National Standard For Electric Lamps—Double-Capped Fluorescent Lamps— Dimensional and Electrical Characteristics* (approved June 29, 2016).

[26] *IEC Standard—Double-capped fluorescent lamps—Performance specifications,* (Amendment 4, Edition 5.0) (approved February 2010).

[27] *IEC Standard—Double Capped Fluorescent Lamps—Performance specifications,* (Amendment 6, Edition 5.0) (approved August 2017).''

[28] ANSI Standard C82.77, *American National Standard—Harmonic Emission Limits—Related Power Quality Requirements* (approved January 17, 2002).

[29] IEC 62301, *Household electrical appliances—Measurement of standby power* (Edition 2.0, 2011–01).

relevant (*i.e.,* LED lighting harmonic current limits and optional power quality metric) to DOE's FLB test procedure. Therefore, in this final rule DOE is adopting the 2002 version of ANSI C82.77 for incorporation by reference.

DOE also received comments on IEC 62301, which it proposed for incorporation by reference for measurements of standby mode power of fluorescent lamp ballasts. These comments are discussed in section III.E of this document, which specifically addresses standby mode and addresses the related comments.

C. Definitions

In the March 2019 NOPR, DOE proposed several updates to definitions related to the FLB test procedure. Currently, ''designed and marketed'' means that the intended application of the lamp is clearly stated in all publicly available documents (*e.g.,* product literature, catalogs, and packaging labels).[30] In the March 2019 NOPR, DOE proposed to specify explicitly that the term also includes the intended application of ballast consistent with the application of the definition of ''designed and marketed'' to fluorescent lamp ballasts. 84 FR 9910, 9917.

DOE also proposed to update definitions for the instant-start, programmed-start, and rapid-start starting methods in appendix Q. Specifically, DOE proposed to add language to these definitions stating that these starting methods are typically indicated on publicly available documents of a fluorescent lamp ballast. DOE finds that this language will provide further guidance in identifying the starting method of the ballast.

Additionally, DOE proposed to remove the following terms in appendix Q that are currently defined but will no longer be used in the revised test procedure: ''AC control signal,'' ''cathode heating,'' ''DC control signal,'' ''F34T12 lamp,'' ''F96T12/ES lamp,'' ''F96T12HO/ES lamp,'' ''PLC control signal,'' and ''wireless control signal.'' ''AC control signal'' and ''DC control signal'' are not reflective of the products currently available on the market, and the rest of the terms are not used in the FLB test procedure.

NEMA and Signify agreed with DOE's proposed removal of unused definitions. (NEMA, No. 3 at p. 3; Signify, No. 7 at p. 3) DOE has determined that the removal of definitions described in this section will improve the clarity of FLB test procedure and will not affect measured values.

Hence, in this final rule DOE is (1) updating the term ''designed and marketed'' in 10 CFR 430.2 to include the intended application of ballasts, (2) updating language in definitions of ''instant-start,'' ''programmed-start,'' and ''rapid-start,'' and (3) removing the following terms in the Definitions section of appendix Q: ''AC control signal,'' ''cathode heating,'' ''DC control signal,'' ''F34T12 lamp,'' ''F96T12/ES lamp,'' ''F96T12HO/ES lamp,'' ''PLC control signal,'' and ''wireless control signal.''

D. Amendments to Active Mode Test Method

1. General

In the March 2019 NOPR, DOE proposed several updates to appendix Q regarding instrumentation, test setup, test conditions, and measurements. DOE also proposed a general instruction in section 2.1 (''Active Mode Procedure'') that specifications in referenced industry standards that are recommended, stated as ''shall'' or ''should'' be met, or that are not clearly mandatory are, for purposes of the DOE test procedure, mandatory (unless they conflict with language in appendix Q) to ensure testing is conducted in a uniform manner by different entities to yield consistent results. 84 FR 9910, 9918. DOE received no comments on this proposed change. DOE has determined this is not a substantive change to the test procedure, and will not change measured values. DOE is adopting section 2.1 as proposed.

2. Instrumentation

In the March 2019 NOPR, DOE proposed to reference section 9 (''Electrical Instruments'') of ANSI C78.375A–2014 in section 2.2 (''Instruments'') of the active mode test procedure instead of referencing ANSI C82.2 generally. The reference to ANSI C82.2 is being updated from the 2002 version to the 2016 version in this final rule. Both versions of ANSI C82.2 reference ANSI C78.375A–1997 but also specify that the latest version of ANSI C78.375 applies. The latest version of ANSI C78.375 (the 2014 version) makes no updates to its electrical instruments section compared to the 1997 version (see section III.B). 84 FR 9910, 9919.

DOE did not receive any comments on these proposed amendments. DOE has determined that directly referencing ANSI C78.375A–2014 improves the readability of the DOE test procedure by identifying subsequently referenced industry standards, that this change does not make substantive changes to the test procedure, and that this amendment will not change measured values. In this final rule, DOE adopts the clarifications regarding references to industry standards in the ''Instrumentation'' section as described in this section.

3. Test Setup

In the March 2019 NOPR, DOE proposed several amendments to section 2.3 (''Test Setup'') of the active mode test procedure in appendix Q. These included: (1) More precisely referencing industry standards, (2) renaming the ''Power Analyzer'' subsection to ''Test Circuits'' and clarifying the specified power analyzer capabilities, (3) clarifying selection of reference lamps, and (4) clarifying instructions for identifying the reference lamp.

a. References to Industry Standards

Section 2.3.1 of the active mode test procedure in appendix Q references ANSI C82.1 and ANSI C78.81 without specific instruction regarding applicability to low- or high-frequency ballasts. In the March 2019 NOPR, DOE proposed to specify use of ANSI C82.1 to test low-frequency ballasts and use of ANSI C82.11 to test high-frequency ballasts. 84 FR 9910, 9918. DOE also proposed to remove the reference to ANSI C78.81, which contains no wiring instructions. *Id.* In conjunction with referencing ANSI C82.1, DOE proposed to add an instruction to disregard section 5.3 (''Ballast Output'') of the standard. *Id.* Section 5.3 of ANSI C82.1 specifies minimum power factor requirements, which may be confused with the minimum power factor requirements set forth in DOE's energy conservation standards for fluorescent lamp ballasts (see 10 CFR 430.32(m)). In referencing ANSI C82.11, DOE proposed to disregard section 5.3.1 (''Ballast Factor'') in the standard because the DOE test procedure does not specify determination of ballast factor. 84 FR 9910, 9918. DOE also proposed to disregard Annex D (''Dimming Ballast Energy Efficiency Test Method'') and section 5.13 (''Ballast Efficiency'') in ANSI C82.11 for the active mode test procedure of measuring BLE at full light output, a metric that is different from ballast efficiency described in these sections. 84 FR 9910, 9918–9919.

DOE did not receive any comments on the proposed amendments. DOE has determined that these updates provide clearer instructions on using referenced

[30] The definition of ''designed and marketed'' is applicable to terms related to the following covered lighting products: Fluorescent lamp ballasts; fluorescent lamps; general service fluorescent lamps; general service incandescent lamps; general service lamps; incandescent lamps; incandescent reflector lamps; medium base compact fluorescent lamps; and specialty application mercury vapor lamp ballasts. 10 CFR 430.2.

industry standards and do not make substantive changes to the test procedure or change measured values. In this final rule, DOE adopts the clarifications regarding references to industry standards in the ''Test Setup'' section as described in this section.

b. Updates to Power Analyzer

In the March 2019 NOPR, DOE also proposed to rename the ''Power Analyzer'' section (section 2.3.2 of appendix Q) to ''Test Circuits'' because it provides instructions regarding not only the power analyzer but also for connecting the power supply, ballast, and lamp in the appropriate circuit. Section 2.3.2.1 of appendix Q requires that the power analyzer must have ''n + 1'' channels where ''n'' is the number of lamps the ballast can operate. In the March 2019 NOPR, DOE also proposed to specify that ''n'' is the maximum number of lamps the ballast is designed and marketed to operate, to ensure that the power analyzer has enough channels. 84 FR 9910, 9918.

DOE did not receive any comments on the proposed amendments. DOE has determined these updates provide clearer instructions regarding the power analyzer setup and do not make substantive changes to the test procedure or change measured values. In this final rule, DOE adopts the clarifications regarding the power analyzer setup as described in this section.

c. Selection of Reference Lamps

As compared to when DOE initially established a test procedure for fluorescent lamp ballasts, the market now offers certain ballasts that each can operate lamps of more than one lamp base type and diameter—for example, ballasts that can operate T5 (miniature bipin), T8 (medium bipin), and T12 lamps (both recessed double contact and slimline). Because appendix Q currently does not specify which reference lamp to select for these types of ballasts, in the March 2019 NOPR, DOE proposed to provide additional direction in appendix Q. First, DOE proposed in newly added section 2.3.3.3 that a ballast designed and marketed to operate lamps of multiple base types, except for sign ballasts, must be tested with one base type in the following order of decreasing preference: Medium bipin, miniature bipin, single pin, and recessed double contact. 84 FR 9910, 9918. Second, DOE proposed in newly added section 2.3.3.4 to require, after selecting the base type, a ballast designed and marketed to operate lamps of multiple diameters must be tested with one diameter in the following order of decreasing preference: T8, T5, or T12. *Id.*

NEMA stated that base type has less influence on efficiency measurements than the number and type of lamps being operated, emphasizing that the number of lamps is more relevant. (NEMA, No. 3 at p. 3) Signify commented that, while DOE's proposed criteria may work, because DOE's efficiency standard for fluorescent lamp ballasts is a function of the ballast circuit and output power, it would be simpler to specify choosing the maximum lamp power for multi-lamp type ballasts. Signify stated that testing for the highest lamp power results in testing for the highest efficiency requirement. Signify added that the ballast will operate at its maximum power with the maximum load regardless of lamp base type. (Signify, No. 7 at pp. 2–4)

DOE based the proposed selection of the base type and diameter of the reference lamp for ballasts that can operate multiple lamp types on the most common products on the market. As noted by commentators, base type does not impact lamp power. However, lamp diameters may impact lamp power. Hence, the order of preference dictated by most common diameter may not always result in selecting the lamp diameter with the maximum lamp power. Testing ballasts that can operate multiple lamp types with the most common lamp type provides test results more appropriately representative of an average period of use. (See, 42 U.S.C. 6293(b)(3)) DOE also notes that, regardless of the selection of base type or diameter, section 2.3.1.4 of appendix Q already requires that the ballast be tested connected to the maximum number of lamps the ballast is designed and marketed to operate.

DOE has determined the updates to the selection of reference lamps for ballasts that can operate more than one lamp type adds consistency and repeatability to the test procedure and do not make substantive changes to the test procedure or change measured values. In this final rule, DOE adopts the selection criteria for reference lamps for ballasts that can operate more than one lamp type as described in this section.

d. Reference Lamp Identification

Section 2.3.1.3 of appendix Q, which pertains to testing in active mode, specifies that the fluorescent lamp used for testing must be a reference lamp as defined in ANSI C82.13 and be seasoned for at least 12 hours. ANSI C82.13 states that reference lamps are ''seasoned lamps which under stable operating conditions and in conjunction with the specified reference ballast operate at'' certain voltage, wattage, and current. In the March 2019 NOPR, DOE proposed further clarification in newly added section 2.3.3.1 that the reference lamp be tested with a reference ballast that meets the criteria of the 2016 version of ANSI C82.3, the industry standard for reference ballasts of fluorescent lamps. ANSI C82.13 also states that reference lamps must meet certain voltage, wattage, and current criteria under stable operating conditions. Hence, DOE also proposed to include the stabilization criteria for reference lamps as specified in newly added section 2.5.2.1 of appendix Q. 84 FR 9910, 9918.

In the March 2019 NOPR, DOE also proposed to remove references to ''rapid-start lamps'' and ''instant-start lamps'' in the ''Ballast Type'' column in Table A. The starting method (*e.g.* rapid start, instant start) is dictated by the type of ballast, and the lamp datasheet referenced by Table A for each lamp type provides the appropriate reference lamp specifications for the applicable starting method. As such, including the lamps' associated starting method in the Ballast Type column of this table is unnecessary and potentially confusing. DOE also proposed changing the title of the table from Table A to Table 1. 84 FR 9910, 9916, 9932.

DOE did not receive any comments on the proposed amendments related to the reference lamps. DOE has determined these updates provide explicit instructions to ensure correct procedures and requirements are followed when identifying a reference lamp that meets the definition in ANSI C82.13. DOE has further determined that these amendments do not make substantive changes to the test procedure or change measured values. In this final rule, DOE adopts the changes relating to identifying reference lamps described in this section.

4. Test Conditions

Section 2.4 of appendix Q, which pertains to the active mode test procedure, generally references ANSI C82.2 for all test conditions. In the March 2019 NOPR, DOE proposed to specifically reference ANSI C82.2–2016 sections 3 ''Pertinent measurements'' and 4 ''Electrical supply characteristics—test ballast measurement circuits.'' DOE also proposed to remove instructions in section 2.4.1 of appendix Q regarding normative references in ANSI C82.2, since DOE proposed directly referencing industry standards when necessary rather than relying generally on the normative references in ANSI C82.2.

Similarly, section 2.4.2 of appendix Q generally references ANSI C78.375 to specify requirements for room temperature and air circulation in the test facility. In the March 2019 NOPR, DOE proposed to specifically reference ANSI C78.375A–2014 section 4, ''Ambient Conditions for Lamp Measurements,'' which contains the appropriate information for temperature and air movement requirements.

DOE did not receive any comments on these proposed amendments. DOE determined that these updates provide more direct references to industry standards, and do not make substantive changes to the test procedure or change measured values. In this final rule, DOE is revising general references to ANSI C82.2 and ANSI C78.375A in section 2.4 of appendix Q to provide more precise references to sections 3 and 4 of ANSI C82.2–2016 and section 4 of ANSI C78.375A–2014, as described in this section.

5. Test Method for Ballast Luminous Efficiency

In the March 2019 NOPR, DOE proposed the following amendments to section 2.5 (''Test Method'') of appendix Q, which pertains to the active mode test procedure: (1) Revising the stabilization procedure, including adding a second stabilization option, and (2) requiring measuring lamp arc current and voltage as root mean square (''RMS'') values.

a. Stabilization Criteria

In response to the June 2015 framework document, Signify (as Philips Lighting) recommended DOE adopt a second stabilization option to use when measuring BLE that was developed by industry stakeholders. (Philips Lighting, Docket EERE–2015–BT–STD–0006, No. 8 at pp. 2–5) This stabilization option was also supported by comments from NEMA and Universal Lighting Technologies (''ULT''). (NEMA, Docket EERE–2015–BT–STD–0006, No. 12 at p. 2; ULT, Docket EERE–2015–BT–STD–0006, No. 6 at p. 2) DOE evaluated the second stabilization option as recommended by Signify and proposed its adoption in the March 2019 TP NOPR (''Option 2''). 84 FR 9910, 9919. The Option 2 stabilization method proposed would incorporate by reference the method in Annex D of ANSI C82.11. Specifically, DOE proposed that stable operating conditions under this option be determined according to steps 1 through 6 of section D.2.1 in Annex D of ANSI C82.11.

NEMA and Signify supported DOE's proposal to allow the Option 2 stabilization method for measuring the BLE of ballasts at full light output, stating it reduces testing burden and data management complexity without affecting the accuracy of energy efficiency measurements. (NEMA, No. 3 at p. 4; Signify, No. 7 at p. 6) NEMA suggested DOE offer both Option 1 and Option 2 stabilization methods because some manufacturers will choose to continue with the Option 1 method. (NEMA, No. 3 at p. 4) ASAP/ACEEE supported use of the optional Option 2 stabilization method so long as it is statistically comparable to the current method. ASAP/ACEEE asked DOE to demonstrate that the two options provide statistically identical results before allowing the Option 2 stabilization method. (ASAP/ACEEE, No. 8 at p. 2)

DOE has determined that the second stabilization method will save overall testing time, particularly when testing large batches of ballasts. In response to the June 2015 framework document, Signify (as Philips Lighting) provided BLE test data using both methods for T5 and T8 rapid start and T8 instant start ballasts. For each type of ballast, Philips tested five units of four different models and provided an average BLE for each model at 120 V and 277 V. (Philips Lighting, Docket EERE–2015–BT–STD–0006, No. 8, pp. 2–5) [31] Because the data did not include total lamp arc power for the ballast models, DOE could not conduct an analysis of how these reported values would comply with FLB standards. DOE did again review and compare the methodologies of the two options. Option 2 is different from Option 1 as follows: (1) Option 2 involves pre-heating the ballast in an oven and pre-burning the lamp with a similar ballast while Option 1 does not; and (2) Option 2 requires reaching stable conditions over a five-minute window while Option 1 requires a four-minute window. DOE has determined the difference between the two methods is not substantive enough to yield different final represented values. Pre-heating the ballast will mainly allow the ballasts to be stabilized more quickly and the difference between a five-minute and four-minute window is minimal. Therefore, DOE has determined that Option 2 only impacts the time it takes to achieve stabilization and does not impact final represented values. In this final rule DOE adopts the second stabilization option (''Option 2'') as described in the March 2019 NOPR.

Currently, section 2.5.1.2.1 of appendix Q requires that lamp arc voltage, current, and power be measured once per second while determining stability. In the March 2019 NOPR, DOE proposed to modify the requirement that lamp arc voltage, current, and power be measured once per second, to require instead that those factors be measured once per minute in the Option 1 stabilization method. The once-per-minute requirement is already incorporated in the Option 2 stabilization method. 84 FR 9910, 9919–9920.

NEMA and Signify supported DOE's proposal to change the sampling frequency from one second to one minute in the Option 1 stabilization method, asserting the change will reduce the data storage needs and associated costs. (NEMA, No. 3 at p. 3; Signify, No. 7 at pp. 4–5) NEMA added that lamp-and-ballast systems have high thermal mass and that temperature does not change quickly, thereby generating redundant data at a per-second sampling frequency. (NEMA, No. 3 at p. 3)

As stated in the March 2019 NOPR, DOE reviewed the stabilization criteria in IES LM–9 (proposed in the Option 2 stabilization method) and tentatively determined that taking measurements once per minute to determine if a fluorescent lamp has stabilized is sufficient to determine if a fluorescent lamp ballast has stabilized. 84 FR 9910, 9919. Therefore, DOE has determined that a per-second sampling frequency is unnecessary and its removal would not impact final steady-state conditions reached. In this final rule, DOE is changing the sampling frequency from one second to one minute in the Option 1 stabilization method.

Section 2.5.1.2 of appendix Q currently requires operating the ballast at full output for at least 15 minutes but no longer than 1 hour until stable operating conditions are reached. In the March 2019 NOPR, DOE stated that it does not find a need to restrict the maximum time required to achieve stable operating conditions and therefore proposed to remove the maximum time of one hour required to achieve stable operating conditions in the Option 1 stabilization method. 84 FR 9910, 9919–9920.

NEMA and Signify supported changing the requirement that fluorescent lamp ballasts cannot be operated for longer than one hour to determine stable operating conditions. NEMA stated that in some cases, especially with ballasts that are

[31] These documents were submitted to the docket of DOE's rulemaking to review energy conservation standards for fluorescent lamp ballasts (Docket No. EERE–2015–BT–STD–0006).

potted,[32] it may take some time for ballast components to reach optimal operating temperature. Signify stated that, for a ballast tested with an amalgam lamp or any other energy saving lamp type, the proposed change may reduce test costs by preventing repeat testing if the system has not stabilized in an hour. (NEMA, No. 3 at pp. 3–4; Signify, No. 7 at p. 5) ASAP/ACEEE expressed concern that lifting the one hour restriction may result in test data being collected before ballasts achieve stable operating conditions. (ASAP/ACEEE, No. 8 at p. 2)

Per both Option 1 and Option 2 stabilization methods, a lamp-ballast system is determined to be stable when the differences in measured values of each lamp arc voltage, current, and power do not exceed one percent over a four-minute moving window. To achieve stabilization, this criterion must be met even if the stabilization period exceeds one hour. Hence, in this final rule DOE is removing the maximum stabilization time requirement, as it is irrelevant in determining whether final steady-state conditions have been reached.

b. Measurements

Based on general industry practice of electrical circuit measurements, DOE has interpreted the measurements for lamp arc current and lamp arc voltage to be RMS values. In the March 2019 NOPR, DOE proposed to make explicit this industry practice. 84 FR 9910, 9920.

DOE did not receive any comments on this proposed amendment. DOE has determined that these updates provide clearer instructions on taking measurements consistent with industry practice and do not make substantive changes to the test procedure or change measured values. In this final rule, DOE adopts the explicit direction that measurements of lamp arc current and lamp arc voltage must be RMS values.

In the March 2019 NOPR, DOE also proposed to amend references to sections of ANSI C82.2 as they pertain to taking measurements. 84 FR 9910, 9920. Specifically, DOE proposed to remove references to sections 3.2.1 and 4 of ANSI C82.2 for measuring input current and voltage. DOE initially determined that 3.2.1 of ANSI C82.2 lists parameters to measure for ballast input operating conditions and provides no measurement specifications and that section 4 of ANSI C82.2 provides electrical supply specifications relevant to test conditions but not measurements. *Id.* DOE also proposed to retain the reference to section 7 of ANSI C82.2, but add instruction to disregard references to Figure 1 and Figure 3, as Figure 1 is not relevant for input power measurements and Figure 3 is unnecessary as it specifies a circuit to measure current in rapid start ballasts, which is already provided in the DOE test procedure. *Id.*

NEMA supported DOE's proposal to replace the existing ANSI C82.2 references stating: Section 3.2.1 referenced the ballast efficiency factor metric and not BLE; and the referenced figures showed separate wattage, voltage and current meters, whereas modern testing facilities would be using power analyzers to take measurements. (NEMA, No. 3 at p. 4) Signify suggested DOE retain section 4, stating that several technical requirements in section 4 affect electrical and energy efficiency measurements. (Signify, No. 7 at p. 7)

DOE agrees that section 4 of ANSI C82.2 is a pertinent section to reference. Because it provides electrical supply specifications, DOE references it in the ''Test Conditions'' section rather than in the ''Test Method'' section of the active mode test procedure. DOE has determined that section 3.2.1 of ANSI C82.2 is unnecessary, as it only lists parameters to measure for ballast input operating conditions but provides no measurement specifications. Regarding the referenced figures, only Figure 2 in ANSI C82.2, which involves measuring a ballast's input voltage and current, is relevant to taking input measurements. Hence, in this final rule, in the ''Test Method'' section of the active mode test procedure, DOE removes references to sections 3.2.1 and 4 for measuring input voltage and input current, and instead specifies section 7 with the exclusion of Figure 1 and Figure 3 for measuring input power, input voltage, and input current.

6. Measuring Ballast Performance at Less Than Full Light Output

In the March 2019 NOPR, DOE assessed comments received in response to the June 2015 framework document regarding measuring the performance of fluorescent lamp ballasts at dimmed light output levels and proposed a method to measure ballast efficiency (''BE'') at reduced light output levels for representations in the marketplace. 84 FR 9910, 9920–9921. The proposed BE measurement was the ballast output power divided by the ballast input power, where the ballast output power includes not only the lamp arc power but also the filament power (*i.e.,* ''cathode power'') and power provided for other features such as networking and sensors. Thus, the proposed BE measurement was different than BLE, which does not include filament power in the ballast output power measurement. The proposal did not require manufacturers to test for and measure BE; but, if a manufacturer were to choose to make representations of BE at reduced light output levels, it would have been required to use the test procedure for the BE metric provided in Annex D of ANSI C82.11–2017. Consistent with Annex D, DOE's proposed test method would have applied only to measurements at light output levels at or greater than 50 percent of full light output and require use of the Option 2 stabilization method (see section III.D.5.a of this document). 84 FR 9910, 9921.

DOE received several comments on the proposed test method for measuring BE at reduced light output levels. NEMA stated that, when dimming a fluorescent lamp ballast, cathode heat must be applied [33] to ensure that the reduction in the arc discharge current does not result in shortened lamp lifetime. NEMA asserted that power required to maintain cathode heat (*i.e.,* cathode power, filament power) must be included in the ballast output power measurement. NEMA added that, because the arc discharge and cathode heating currents flow through the same wire and low levels of power are being measured, it is not possible to make reliable measurements below 50 percent light output. (NEMA, No. 3 at p. 4) Signify supported DOE's proposed test method for BE, stating that the test procedures in ANSI C82.11–2014 provide a high level of accuracy and repeatability for measurements at 50 percent and full light output. (Signify, No. 7 at p. 6)

NEMA described a multi-channel measurement approach for BE testing that relies on 13 time-synchronized channels for a 4-lamp fluorescent lamp ballast to capture the input and output power in the same time interval. NEMA stated this approach would require (1) three power analyzers, each costing about $20,000, as most power analyzers have a maximum of six channels, and (2) a test management computer system and software costing about $5,000 to control and synchronize the analyzers. NEMA stated that, while some labs may have this equipment, others may not and may choose not to make the expenditure; resulting in some manufacturers not making BE

[32] In electronics, ''potting'' refers to the process of filling an electronic assembly with a solid or gelatinous compound to provide shock and vibration resistance, as well as protection against moisture and corrosion.

[33] NEMA referenced NEMA Standard LL–9 2011 for guidance related to cathode heat requirements during dimming.

representations of some or all of their products that may require it. (NEMA, No. 3 at p. 5) Signify stated that the test method for measuring BE at reduced light outputs does not necessarily require purchasing new equipment, as power analyzers are also used to measure BLE. Signify explained that the test method can be implemented utilizing (1) a dedicated multi-channel power analyzer, (2) two or more power analyzers used simultaneously, or (3) one power analyzer measuring one lamp port at a time. Signify noted that a multi-channel power analyzer can cost between $2,200 to $20,000, which is comparable to a power analyzer. Signify also stated that the test method for measuring BE would already be adopted by any lab that is accredited to National Voluntary Laboratory Accreditation Program and that tests ballasts at reduced light output levels per ANSI standards. (Signify, No. 7 at pp. 9, 13–14)

Lutron asserted that the efficiency measurement of ballasts at reduced light outputs specified in ANSI C82.11–2014 is slightly different than that required to meet CEC's Title 20 energy efficiency regulations for deep-dimming [34] fluorescent lamp ballasts, and therefore may require significant re-testing without resulting in any energy savings. Lutron added that testing efficiency at reduced light output will be very expensive, as it requires highly specialized equipment and third-party labs will be able to test only a few samples per day. Lutron also noted that the test method for measuring BE at reduced light outputs had been available in ANSI C82.11 since 2014, giving manufacturers ample opportunity to begin publishing such efficiencies. Lutron stated it did not foresee an equivalent DOE test method to increase the use of this metric, as manufacturers are no longer investing in fluorescent technology. (Lutron, No. 6 at pp. 2–3)

CEC and CA IOUs stated that DOE's proposed BE metric is an inappropriate measurement of efficiency at reduced light outputs, as it does not count cathode power used at lower light outputs as a loss. (CA IOUs, No. 5 at p. 1; CEC, No. 4 at p. 1) CEC stated that, while certain dimming levels require cathode heating to protect against lamp failure, this is not necessary at all dimming levels. (CEC, No. 4 at p. 2) CA IOUs stated that the BE metric would result in falsely high efficiency ratings, and CEC asserted that the BE metric would allow any amount of cathode power to be used, whether necessary or not. (CA IOUs, No. 5 at p. 1; CEC, No. 4 at p. 2)

ASAP/ACEEE stated that energy efficiency ratings for dimmable ballasts should reflect both the light level output at which a ballast must provide cathode power to sustain lamp ignition and the efficiency of the ballast to illuminate the lamp. They recommended DOE review comments submitted by CEC to revise the proposed BE test method. (ASAP/ACEEE, No. 8 at pp. 1–2) CA IOUs stated that, while cathode power is required at lower lamp currents, it is not necessary at typical lamp currents nearer to full output, and multiple manufacturers employ cathode ''cut out'',[35] which removes cathode power when it is not required. CA IOUs stated that cathode cut out can result in significant energy savings and should be considered a key metric for determining ballast efficiency. CA IOUs added this can only be done using the BLE metric at low light output levels. CA IOUs stated DOE should include testing for both BE and BLE regardless of light output level. (CA IOUs, No. 5 at pp. 3–4)

CEC also suggested alternative options including (1) requiring measurement of both ballast BLE and BE for any performance measurements at light levels less than 100 percent, (2) requiring the BLE measurement at the light level output just above the threshold where cathode heating would be necessary as well as at light levels above this threshold, and measurement of BE at light outputs below this level,[36] or (3) an alternative method that allows for the amount of, and cut-in light level output point of, cathode power to be measured. (CEC, No. 4 at pp. 1–3)

ASAP/ACEEE expressed concern that DOE's proposed test method does not specifically measure cathode power at any light output less than 100 percent. (ASAP/ACEEE, No. 8 at pp. 1–2) CEC added that the technical challenges to measuring the BLE at light output levels less than 50 percent should not be a reason for DOE to not develop appropriate efficiency metrics and standards for dimming ballasts. (CEC, No. 4 at pp. 3–4)

DOE is maintaining the metric of BLE at full light output for representations and for determining compliance with the current energy conservation standards. The BLE metric accounts for cathode power as a loss because DOE's test procedure isolates lamp arc voltage by capturing cathode power in the input power measurement, but not in the output power measurement (which is quantified as total lamp arc power). 76 FR 25216 (May 4, 2011). Therefore, all else being equal, ballasts that use cathode power are measured as less efficient at full light output than those that do not because cathode power increases the measured input power but not the measured total lamp arc power.

Based on further consideration, including the comments received, DOE is not adopting a BE test method. DOE proposed the BE measurement to include cathode power in ballast output power to account for its necessary use at reduced light output levels. Regarding determining at what light output level cathode power is necessary, manufacturers can apply different cathode cut out designs. DOE does not have data on the light output levels at which cathode power is applied and current product marketing material does not specify the cathode cut out light output level. The industry standard, NEMA Standard LL9–2011, specifies minimum and maximum voltages across cathodes in dimmed operation. However, incorporating such parameters in a metric may influence manufacturer choice as to cathode cut designs that can be employed in fluorescent lamp ballasts. A lamp and ballast manufacturer may be able to employ only the minimum amount of cathode power necessary because the lamp can be designed to only require the minimum amount of cathode power, while a manufacturer that produces only ballasts may have to provide more cathode power to ensure that its ballasts can operate all lamps since the minimum amount of cathode power required can vary by lamp. DOE finds that it is important to allow for flexibility in designing ballasts, and a metric should not favor one approach over another.

Given these issues the proposed BE test method may not provide an accurate representation of efficiency for all dimmable ballasts at all reduced light outputs. DOE is not aware of an industry standard at this time that provides a test method to accurately capture the efficiency of a ballast at reduced light output levels. Additionally, current energy conservation standards for fluorescent lamp ballasts do not require efficiency measurements at lower light outputs. Because the proposed BE test method may not provide the most accurate representations, and such a test method is not necessary for compliance, DOE is

[34] ''Deep-dimming fluorescent lamp ballast'' means a fluorescent ballast that is capable of operating lamps in dimmed operating modes at any number of levels at or below 50 percent of full output. California Title 20 Appliance Efficiency Regulations.

[35] The term ''cut out'' refers to removing all power to the lamp electrodes after lamp ignition.

[36] CEC suggested using NEMA Standard LL9–2011, section 2.2 to develop this method.

not adopting a test method for measuring ballast efficiency at reduced light outputs in this final rule.

E. Amendments to Standby Mode Test Method

Currently, the measurement of standby mode power is not required to determine compliance with energy conservation standards for fluorescent lamp ballasts. However, if a manufacturer chooses to make any representations with respect to the standby mode power use of fluorescent lamp ballasts, section 3 of appendix Q requires standby mode power testing to be performed in accordance with ANSI C82.2.

EPCA directs DOE to establish test procedures to include standby mode energy consumption, ''taking into consideration the most current versions of Standards 62301 and 62087 of the International Electrotechnical Commission[.]'' (42 U.S.C. 6295(gg)(2)(A)) IEC Standard 62087 applies only to audio, video, and related equipment, and therefore is not relevant to lighting products. The current standby mode test procedure is consistent with procedures outlined in IEC Standard 62301, which applies generally to household electrical appliances. 74 FR 54445, 54449 (Oct. 22, 2009). To provide a test method that would be familiar to FLB manufacturers at the time the standby mode test procedure was initially established, DOE referenced language and methodologies presented in 2002 edition of ANSI C82.2. *Id.*

In the March 2019 NOPR, DOE proposed requiring stabilization and subsequent measurement of standby mode energy consumption according to the measurements in section 5 of IEC 62301 (edition 2.0), instead of ANSI C82.2. IEC 62301, which applies generally to household electrical appliances, provides requirements specifically for measuring standby mode energy consumption, whereas ANSI C82.2 does not. For consistency within the test procedure and to reduce the test burden, DOE also proposed that the appendix Q requirements for instruments, test setup and test conditions for the active mode test procedure be followed for standby power measurements. (This includes direction regarding the input voltage at which to test when the ballast can operate at multiple input voltages, which is not currently specified by the current test conditions referenced in ANSI C82.2.) Furthermore, unlike the active mode test procedure, DOE proposed not to require use of reference lamps because lamps are not turned on during the measurement of standby mode power consumption. Additionally, DOE proposed that whatever lamp to which the ballast is connected be turned on initially at full light output for the purpose of ensuring the ballast is not defective. 84 FR 9910, 9921–9922.

NEMA stated that DOE should not incorporate IEC 62301 at this time, as the IEC is currently working on lighting-specific standards and adoption of a less-appropriate method of measurement could negatively impact the product sector. (NEMA, No. 3 at p. 5) Similarly, Signify suggested DOE should wait for either ANSI or IEC to publish a standby power test method for fluorescent lamp ballasts, and noted that IEC is currently considering developing a standby power test method for lighting devices based on IEC 62301, but that the committee found it necessary to make some changes, explanations, and adaptations to the appliances standby power test method provided in IEC 62301. (Signify, No. 7 at p. 8) Lutron agreed with NEMA's comments that, if DOE needs to reference a standard for standby power, it should wait to reference the lighting-specific IEC standard under development. Lutron further stated in its written comments that during the public meeting for the Process Rule,[37] stakeholder discussion had included the possibility that test procedures may need to be updated quickly with the consensus of all stakeholders. Lutron stated that such a consensus could be achievable for adopting a lighting-specific IEC standard for FLB standby mode power measurements. (Lutron, No. 6 at p. 3)

Fluorescent lamp ballasts are included in the scope of the IEC 63201, which applies to electrical products with a rated input voltage between 100 V a.c. to 250 V a.c. for single phase products and 130 V a.c. to 480 V a.c. for other products. DOE has determined that the instructions and criteria specified in IEC 62301 for stabilization and subsequent measurement of standby mode power consumption are appropriate for fluorescent lamp ballasts. DOE has not received any comments specifying technical reasons as to why the use of IEC 62301 would not result in representative FLB standby mode power measurements. Moreover, IEC 62301 provides specific instruction regarding the measurement of standby power, whereas the currently referenced industry test procedure, ANSI C82.2, does not. DOE is largely maintaining the same instruments, test setup, and test conditions to measure standby mode power as are used to measure active mode power; these requirements are largely contained in ANSI C82.2. IEC 62301 is only referenced regarding stabilization and when taking the actual power measurement as the stabilization and power measurement of a ballast that is not operating a lamp is not included in ANSI C82.2.

DOE acknowledges that industry is in the process of developing a lighting-specific standby mode power test method, but at the present, no such industry standard has been issued. DOE will review any such industry standby mode power test method once it becomes available. At this time, DOE has determined that IEC 62301 is more appropriate for measuring standby mode power than the currently referenced ANSI C82.2, which makes no mention of standby mode power. As such DOE is amending appendix Q to reference IEC 62301 in place of ANSI C82.2 for the measurement of standby mode power consumption.

CEC supported DOE's proposed standby mode test method if it explicitly captures ballast features not associated with light output such as networking and sensors. (CEC, No. 4 at p. 4) ASAP/ACEEE also supported the recommendation of the CA IOUs provided in response to the June 2015 framework document[38] that ballasts with communication and control capabilities be tested with the ballasts connected to a network and with communication and control capabilities enabled. (ASAP/ACEEE, No. 8 at pp. 2–3)

Section 3.2.1 of appendix Q specifies that, if standby mode power is measured, fluorescent lamp ballasts that are designed and marketed for connection to control devices must be tested with all commercially available compatible control devices connected in all possible configurations. DOE is maintaining this instruction in this final rule as it sufficiently addresses connection of all features necessary for the operation of the fluorescent lamp ballast designed and marketed to connect to control devices.

ASAP/ACEEE requested DOE provide the technical basis for DOE's initial determination in the March 2019 NOPR that specific lamps to which the ballast is connected do not affect standby mode energy, as well as the applicability to all

[37] Information regarding the Process Rule can be found on *https://www.regulations.gov,* Docket number EERE–2017–BT–STD–0062–0163 at *https://www.regulations.gov/document?D=EERE-2017-BT-STD-0062-0163.*

[38] ASAP/ACEEE referenced the CA IOUs comment submitted under Docket No. EERE–2015–BT–STD–0006.

fluorescent lamp ballasts. (ASAP/ACEEE, No. 8 at pp. 2–3)

Regarding connection of lamps, DOE tested the standby mode power consumption of certain digital ballasts with 1 to 3 different types of controllers with and without lamps connected to the ballast. Table III.2 shows standby mode power consumption measurements for a ballast and controller combination with and without lamps connected and differences in power consumption.

TABLE III.2—STANDBY MODE POWER CONSUMPTION WITH AND WITHOUT LAMPS

Ballast and controller combination	Standby power consumption with lamps (mW)	Standby power consumption without lamps (mW)	Difference in standby power consumption (mW)
1	595	590	5
2	590	591	−1
3	592	592	0
4	91.9	87.5	4.4
5	91.2	86.6	4.6
6	88.3	87.1	1.2
7	903	904	−1

DOE found that the difference in standby mode power consumption with lamps versus without lamps ranged from 0 milliwatts (''mW'') to 5 mW. These differences are within general tolerances of measurements. Per IEC 62301 section 5, for products that have power measurements equal to or less than 1 W, stability is achieved when the power difference is at or less than 10 mW/h across a certain time period. Using the stability criteria of 10 mW/h as a general guideline for expected fluctuations in measurements, DOE finds differences in observed power measurements with lamps versus without lamps to be de minimis. Hence, DOE has determined that testing with or without a lamp does not impact measured values and therefore, the lamp connected to the ballast does not impact measured values. Further, standby power consumption is measured after lamps at full light output are turned off. In this state, the power being consumed by the ballast cannot be applicable to the lamp, as fluorescent lamps do not have any features that consume standby power, nor is there any residual power consumption from the lamp having been turned on.

ASAP/ACEEE also suggested the standby mode test procedure reference the active mode test procedure sections pertaining to instrumentation and connection of lamps. (ASAP/ACEEE, No. 8 at pp. 2–3) As stated previously, DOE is applying the requirements in the active mode test procedure for instrumentation and test setup to the standby power measurements.

DOE has determined that the proposed amendments to the standby mode energy consumption test procedure provide further clarity to the test steps by referencing a more appropriate industry standard for the actual measurement of power and that the proposed amendments do not affect measured values. Therefore, in this final rule, DOE adopts the amendments to the standby mode test procedure for fluorescent lamp ballasts as described in this section.

F. Amendments to 10 CFR 430.23(q)

In the March 2019 NOPR, DOE proposed to remove paragraphs specifying the calculation of estimated annual energy consumption and estimated annual operating cost for fluorescent lamp ballasts in 10 CFR 430.23(q), as these calculations are not required by DOE or the Federal Trade Commission. DOE also proposed to add a paragraph in 10 CFR 430.23(q) to calculate power factor using appendix Q. 84 FR 9910, 9922. Signify supported DOE's proposal to include a description of power factor calculation and remove calculations for estimated annual energy consumption and annual operating cost. (Signify, No. 7 at p. 8)

DOE has determined that these proposed updates to 10 CFR 430.23(q) provide further clarification and would not impact current requirements of the DOE test procedure or measured values. In this final rule DOE adopts the changes to 10 CFR 430.23(q) described in this section.

G. Amendments to 10 CFR 429.26

In the March 2019 NOPR, DOE proposed explicitly requiring reporting average total lamp arc power in certification reports for fluorescent lamp ballasts. Average total lamp arc power, a value that is already determined in appendix Q, is necessary to determine the required minimum BLE for an FLB model. Manufacturers are already reporting average total lamp arc power when certifying basic models, thus, DOE does not expect any changes in burden. DOE also proposed to require that average total lamp arc power be rounded to the nearest tenth of a watt. Additionally, DOE proposed to specify that the represented value of average total lamp arc power must be equal to the mean of the sample. Finally, DOE proposed to remove ''annual energy operating costs'' in 10 CFR 429.26(a)(2)(i), as this value is not required by DOE or the Federal Trade Commission. 84 FR 9910, 9922.

DOE did not receive any comments on the proposed amendments to the reporting requirements. DOE has determined that these proposed updates to 10 CFR 429.26 provide further clarification and would not impact current requirements of the DOE test procedure, change measured values, or change the current reporting burden. In this final rule, DOE adopts the changes to 10 CFR 429.26 described in this section.

H. Effective and Compliance Dates

The effective date for the adopted test procedure amendment is October 14, 2020. EPCA prescribes that all representations of energy efficiency and energy use, including those made on marketing materials and product labels, must be made in accordance with an amended test procedure, beginning 180 days after publication of the final rule in the **Federal Register**. (42 U.S.C. 6293(c)(2)) EPCA provides an allowance for individual manufacturers to petition DOE for an extension of the 180-day period if the manufacturer may experience undue hardship in meeting the deadline. (42 U.S.C. 6293(c)(3)) To receive such an extension, petitions must be filed with DOE no later than 60 days before the end of the 180-day period and must detail how the manufacturer will experience undue hardship. (*Id.*)

I. Test Procedure Costs and Impact

EPCA requires that test procedures adopted by DOE not be unduly burdensome to conduct. In this final rule, DOE amends the existing test procedure for fluorescent lamp ballasts by providing a second stabilization option for measuring BLE. The amendments also: (1) Update references to industry standards; (2) clarify the selection of reference lamps; (3) remove extraneous requirements in the stabilization procedure; and (4) revise the test procedure for measuring standby mode energy consumption. DOE has determined that the test procedure as amended by this final rule will not be unduly burdensome for manufacturers to conduct and instead will decrease the test burden for manufacturers.

This final rule will result in a net cost savings to manufacturers, as presented in Table III.3 and Table III.4 of this document.

TABLE III.3—SUMMARY OF COST IMPACTS FOR FLUORESCENT LAMP BALLASTS

Category	Present value (thousand 2016$)	Discount rate (percent)
Cost Savings:		
Reduction in Future Testing Costs	74	3
	28	7
Total Net Cost Impact:		
Total Net Cost Impacts	(74)	3
	(28)	7

TABLE III.4—SUMMARY OF ANNUALIZED COST IMPACTS FOR FLUORESCENT LAMP BALLASTS

Category	Annualized value (2016$)	Discount rate (percent)
Cost Savings:		
Reduction in Future Testing Costs	2,222	3
	1,982	7
Total Net Cost Impact:		
Total Net Cost Impacts	(2,222)	3
	(1,982)	7

Further discussion of the cost impacts of the test procedure amendments are presented in the following paragraphs.

a. Option 2 Stabilization Method

In this final rule, DOE is allowing manufacturers to use a second stabilization option (*i.e.,* ''Option 2'') when measuring BLE. As described in section III.D.5.a, the Option 2 stabilization method would minimize the time the test lamps are off, thereby reducing the stabilization time and, consequently, the overall testing time. DOE estimates the cost savings of the Option 2 stabilization method to be $2,519 annually. This estimate is based on a savings of 15 minutes per ballast test (due to reduced stabilization time). Inputs to the calculation were updated in this notice to reflect the most recent known values. Based on a median hourly labor rate of $40.96 [39] per electrical engineering technician (this includes an inflation factor of 31 percent to account for the cost of providing benefits), DOE estimates the savings to be $10.24 per ballast test, or $40.96 per basic model, assuming four ballast tests per basic model. DOE does not expect all manufacturers to choose to use the Option 2 stabilization method. Based on the manufacturers that already possess the equipment necessary for Option 2 (*i.e.,* an oven for ballasts), DOE estimates that only four manufacturers (comprising about 18 percent of FLB manufacturers) will choose to utilize the Option 2 stabilization method. DOE estimates that these manufacturers combined offer about 246 basic models of fluorescent lamp ballasts, comprising about 54 percent of all basic models certified in DOE's Compliance Certification Database.[40] New basic models of fluorescent lamp ballasts are introduced and certified to DOE about once every four years. Thus, DOE estimates overall annualized industry savings due to proposing the Option 2 stabilization method to be $2,222 at a 3 percent discount rate and $1,982 at a 7 percent discount rate. In summary, DOE's analysis indicates that allowing the Option 2 stabilization method would result in a reduction of future testing (see Table III.3 and Table III.4).

DOE has determined that the amendment to allow manufacturers to use the Option 2 stabilization method will not require changes to the designs of fluorescent lamp ballasts, and that the amendments will not impact the utility of such product or impact the availability of available FLB options. The amendments will not impact the representations of FLB energy efficiency. Manufacturers will be able to rely on data generated under the test procedure in effect prior to the adoption of this amendment. As such, retesting of fluorescent lamp ballasts will not be required solely as a result of DOE's adoption of this amendment to the test procedure.

b. Additional Amendments

The remainder of the amendments adopted in this final rule will not impact test costs: (1) Updating references to industry standards; (2) clarifying the selection of reference lamps; (3) removing extraneous requirements in the stabilization procedure; and (4) revising the test procedure for measuring standby mode energy consumption.

[39] Bureau of Labor Statistics, Occupational Employment Statistics, available at: *https://www.bls.gov/oes/current/oes173023.htm (May 2018).* Last accessed January 9, 2020.

[40] DOE's Compliance Certification Database is available at *https://www.regulations.doe.gov/certification-data/#q=Product_Group_s%3A**. Last accessed January 9, 2020.

First, in this final rule, DOE is incorporating by reference newer versions of already referenced industry standards in DOE's FLB test procedure (see section III.B). Regarding the adoption of the latest versions of industry standards, Signify stated that there would hardly be any additional burden to a testing facility that has been accredited to the current edition of ANSI standards, and further the use of the latest versions would keep testing facilities up-to-date on current technologies and provide access to more modern test methods. (Signify, No.7, p. 14)

Second, in this final rule, DOE is providing additional clarifications on how to select reference lamps to address, in particular, new products on the market (*i.e.,* ballasts that can operate multiple lamp types) (see section III.D.3.c). The additional direction on selecting reference lamps reflects the current FLB market.

Third, this final rule removes a maximum operating time for stabilization and changes the requirement to take measurements from once per second to once per minute during the stabilization process (see section III.D.5.a). DOE finds that these changes to the stabilization process will have no impact on costs or test burden. Removing the maximum operating time may prevent the restart of the stabilization procedure in certain cases, but due to the unpredictable nature, DOE is unable to quantify how many products may experience an increase or decrease in stabilization time. The reduction in the frequency (*i.e.,* seconds to minute) of measuring data during stabilization will reduce the amount of data required to determine stabilization. However, because this data is collected electronically, changing the measurement frequency results in no cost savings based on time and labor.

Finally, for taking standby mode measurements in this final rule, DOE changes the industry standard reference from ANSI C82.2 to IEC 62301 Section 5; specifies that use of reference lamps is not required; and aligns instrumentation, test setup, and test conditions for taking active mode measurements with standby mode measurements (see section III.E). IEC 62301 Section 5 provides detailed instructions but does not change the overall method of obtaining power measurements and does not require new or additional instrumentation. Currently manufacturers are not making representations of standby power mode.

DOE has determined that the amendments described above do not require additional measurements, steps, or instruments, and therefore will have no impact on cost. Manufacturers will be able to rely on data generated under the test procedure in effect prior to the adoption of this amendment.

IV. Procedural Issues and Regulatory Review

A. Review Under Executive Order 12866

The Office of Management and Budget (''OMB'') has determined that this test procedure rulemaking does not constitute a ''significant regulatory action'' under section 3(f) of Executive Order 12866, Regulatory Planning and Review, 58 FR 51735 (Oct. 4, 1993). Accordingly, this action was not subject to review under the Executive order by the Office of Information and Regulatory Affairs (''OIRA'') in OMB.

B. Review Under Executive Orders 13771 and 13777

On January 30, 2017, the President issued Executive Order (E.O.) 13771, ''Reducing Regulation and Controlling Regulatory Costs.'' E.O. 13771 stated the policy of the executive branch is to be prudent and financially responsible in the expenditure of funds, from both public and private sources. E.O. 13771 stated it is essential to manage the costs associated with the governmental imposition of private expenditures required to comply with Federal regulations.

Additionally, on February 24, 2017, the President issued E.O. 13777, ''Enforcing the Regulatory Reform Agenda.'' E.O. 13777 required the head of each agency designate an agency official as its Regulatory Reform Officer (''RRO''). Each RRO oversees the implementation of regulatory reform initiatives and policies to ensure that agencies effectively carry out regulatory reforms, consistent with applicable law. Further, E.O. 13777 requires the establishment of a regulatory task force at each agency. The regulatory task force is required to make recommendations to the agency head regarding the repeal, replacement, or modification of existing regulations, consistent with applicable law. At a minimum, each regulatory reform task force must attempt to identify regulations that:

(i) Eliminate jobs, or inhibit job creation;

(ii) Are outdated, unnecessary, or ineffective;

(iii) Impose costs that exceed benefits;

(iv) Create a serious inconsistency or otherwise interfere with regulatory reform initiatives and policies;

(v) Are inconsistent with the requirements of Information Quality Act, or the guidance issued pursuant to that Act, in particular those regulations that rely in whole or in part on data, information, or methods that are not publicly available or that are insufficiently transparent to meet the standard for reproducibility; or

(vi) Derive from or implement Executive Orders or other Presidential directives that have been subsequently rescinded or substantially modified.

DOE concludes that this rulemaking is consistent with the directives set forth in these executive orders. This final rule is estimated to result in a cost savings. The final rule yields annualized cost savings of approximately $1,982 using a perpetual time horizon discounted to 2016 at a 7 percent discount rate. Therefore, this final rule is an E.O. 13771 deregulatory action.

C. Review Under the Regulatory Flexibility Act

The Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) requires preparation of a final regulatory flexibility analysis (''FRFA'') for any final rule where the agency was first required by law to publish a proposed rule for public comment, unless the agency certifies that the rule, if promulgated, will not have a significant economic impact on a substantial number of small entities. As required by Executive Order 13272, ''Proper Consideration of Small Entities in Agency Rulemaking,'' 67 FR 53461 (August 16, 2002), DOE published procedures and policies on February 19, 2003 to ensure that the potential impacts of its rules on small entities are properly considered during the DOE rulemaking process. 68 FR 7990. DOE has made its procedures and policies available on the Office of the General Counsel's website: *http://energy.gov/gc/office-general-counsel.* DOE certified in the March 2019 NOPR that the adopted amendments will not have a significant economic impact on a substantial number of small entities. The factual basis of this certification is set forth in the following paragraphs.

The Small Business Administration (''SBA'') considers a business entity to be a small business, if, together, with its affiliates, it employs less than a threshold number of workers specified in 13 CFR part 121. These size standards and codes established by the North American Industry Classification System (''NAICS'') and are available at *https://www.sba.gov/document/support--table-size-standards.* FLB manufacturing is classified under NAICS 335311, ''Power, Distribution, and Specialty Transformer Manufacturing.'' The SBA sets a threshold of 750 employees or fewer for an entity to be considered as a small business for this category.

To estimate the number of companies that could be small businesses that manufacture these ballasts, DOE conducted a market survey using publicly available information. DOE's research involved reviewing information provided by trade associations (*e.g.,* NEMA), information from individual company websites, market research tools (*i.e.,* Hoover's reports) and DOE's Certification Compliance Database. DOE screened out companies that do not meet the definition of a ''small business'' or are completely foreign owned and operated. DOE identified no small businesses that manufacture fluorescent lamp ballasts in the United States. DOE requested comment on its tentative determination that there are no small businesses that manufacture fluorescent lamp ballasts in the United States. NEMA was not aware of any small businesses that manufacture fluorescent lamp ballasts in the United States. (NEMA, No. 3 at pp. 5–6) Signify stated that it did not have sufficient data to comment on this topic. (Signify, No. 7 at p. 16)

Based on the criteria outlined earlier and the reasons discussed in this section, DOE previously certified in the March 2019 TP NOPR that the amendments adopted in this final rule will not have a significant economic impact on a substantial number of small entities. The factual basis for this certification has not changed. Therefore, DOE concludes that the cost effects accruing from the final rule would not have a ''significant economic impact on a substantial number of small entities,'' and that the preparation of a FRFA is not warranted. DOE has submitted a certification and supporting statement of factual basis to the Chief Counsel for Advocacy of the Small Business Administration for review under 5 U.S.C. 605(b).

D. Review Under the Paperwork Reduction Act of 1995

Manufacturers of fluorescent lamp ballasts must certify to DOE that their products comply with any applicable energy conservation standards. To certify compliance, manufacturers must first obtain test data for their products according to the DOE test procedures, including any amendments adopted for those test procedures. DOE has established regulations for the certification and recordkeeping requirements for all covered consumer products and commercial equipment, including fluorescent lamp ballasts. (See generally 10 CFR part 429.) The collection-of-information requirement for the certification and recordkeeping is subject to review and approval by OMB under the Paperwork Reduction Act (''PRA''). This requirement has been approved by OMB under OMB control number 1910–1400. Public reporting burden for the certification is estimated to average 35 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.

DOE is adopting slight modifications to the reporting requirements for fluorescent lamp ballasts. DOE received no comments on its proposal and has determined that these updates to 10 CFR 429.26 do not impact current reporting burden.

Notwithstanding any other provision of the law, no person is required to respond to, nor shall any person be subject to a penalty for failure to comply with, a collection of information subject to the requirements of the PRA, unless that collection of information displays a currently valid OMB Control Number.

E. Review Under the National Environmental Policy Act of 1969

In this final rule, DOE establishes test procedure amendments that it expects will be used to develop and implement future energy conservation standards for fluorescent lamp ballasts. DOE has determined that this rule falls into a class of actions that are categorically excluded from review under the National Environmental Policy Act of 1969 (42 U.S.C. 4321 *et seq.*) and DOE's implementing regulations at 10 CFR part 1021. Specifically, DOE has determined that adopting test procedures for measuring energy efficiency of consumer products and industrial equipment is consistent with activities identified in 10 CFR part 1021, appendix A to subpart D, A5 and A6. Accordingly, neither an environmental assessment nor an environmental impact statement is required.

F. Review Under Executive Order 13132

Executive Order 13132, ''Federalism,'' 64 FR 43255 (August 4, 1999), imposes certain requirements on agencies formulating and implementing policies or regulations that preempt State law or that have federalism implications. The Executive order requires agencies to examine the constitutional and statutory authority supporting any action that would limit the policymaking discretion of the States and to carefully assess the necessity for such actions. The Executive order also requires agencies to have an accountable process to ensure meaningful and timely input by State and local officials in the development of regulatory policies that have federalism implications. On March 14, 2000, DOE published a statement of policy describing the intergovernmental consultation process it will follow in the development of such regulations. 65 FR 13735. DOE examined this final rule and determined that 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. EPCA governs and prescribes Federal preemption of State regulations as to energy conservation for the products that are the subject of this final rule. States can petition DOE for exemption from such preemption to the extent, and based on criteria, set forth in EPCA. (42 U.S.C. 6297(d)) No further action is required by Executive Order 13132.

G. Review Under Executive Order 12988

Regarding the review of existing regulations and the promulgation of new regulations, section 3(a) of Executive Order 12988, ''Civil Justice Reform,'' 61 FR 4729 (Feb. 7, 1996), imposes on Federal agencies the general duty to adhere to the following requirements: (1) Eliminate drafting errors and ambiguity; (2) write regulations to minimize litigation; (3) provide a clear legal standard for affected conduct rather than a general standard; and (4) promote simplification and burden reduction. Section 3(b) of Executive Order 12988 specifically requires that Executive agencies make every reasonable effort to ensure that the regulation (1) clearly specifies the preemptive effect, if any; (2) clearly specifies any effect on existing Federal law or regulation; (3) provides a clear legal standard for affected conduct while promoting simplification and burden reduction; (4) specifies the retroactive effect, if any; (5) adequately defines key terms; and (6) addresses other important issues affecting clarity and general draftsmanship under any guidelines issued by the Attorney General. Section 3(c) of Executive Order 12988 requires Executive agencies to review regulations in light of applicable standards in sections 3(a) and 3(b) to determine whether they are met or it is unreasonable to meet one or more of them. DOE has completed the required review and determined that, to the extent permitted by law, this final rule meets the relevant standards of Executive Order 12988.

H. Review Under the Unfunded Mandates Reform Act of 1995

Title II of the Unfunded Mandates Reform Act of 1995 (''UMRA'') requires each Federal agency to assess the effects of Federal regulatory actions on State, local, and Tribal governments and the private sector. Public Law 104–4, sec. 201 (codified at 2 U.S.C. 1531). For a regulatory action resulting in a rule that may cause 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 (adjusted annually for inflation), section 202 of UMRA requires a Federal agency to publish a written statement that estimates the resulting costs, benefits, and other effects on the national economy. (2 U.S.C. 1532(a), (b)) The UMRA also requires a Federal agency to develop an effective process to permit timely input by elected officers of State, local, and Tribal governments on a proposed ''significant intergovernmental mandate,'' and requires an agency plan for giving notice and opportunity for timely input to potentially affected small governments before establishing any requirements that might significantly or uniquely affect small governments. On March 18, 1997, DOE published a statement of policy on its process for intergovernmental consultation under UMRA. 62 FR 12820; also available at *http://energy.gov/gc/office-general-counsel.* DOE examined this final rule according to UMRA and its statement of policy and determined that the rule contains neither an intergovernmental mandate, nor a mandate that may result in the expenditure of $100 million or more in any year, so these requirements do not apply.

I. Review Under the Treasury and General Government Appropriations Act, 1999

Section 654 of the Treasury and General Government Appropriations Act, 1999 (Pub. L. 105–277) requires Federal agencies to issue a Family Policymaking Assessment for any rule that may affect family well-being. This final rule will not have any impact on the autonomy or integrity of the family as an institution. Accordingly, DOE has concluded that it is not necessary to prepare a Family Policymaking Assessment.

J. Review Under Executive Order 12630

DOE has determined, under Executive Order 12630, ''Governmental Actions and Interference with Constitutionally Protected Property Rights'' 53 FR 8859 (March 18, 1988), that this regulation will not result in any takings that might require compensation under the Fifth Amendment to the U.S. Constitution.

K. Review Under Treasury and General Government Appropriations Act, 2001

Section 515 of the Treasury and General Government Appropriations Act, 2001 (44 U.S.C. 3516 note) provides for agencies to review most disseminations of information to the public under guidelines established by each agency pursuant to general guidelines issued by OMB. OMB's guidelines were published at 67 FR 8452 (Feb. 22, 2002), and DOE's guidelines were published at 67 FR 62446 (Oct. 7, 2002). DOE has reviewed this final rule under the OMB and DOE guidelines and has concluded that it is consistent with applicable policies in those guidelines.

L. Review Under Executive Order 13211

Executive Order 13211, ''Actions Concerning Regulations That Significantly Affect Energy Supply, Distribution, or Use,'' 66 FR 28355 (May 22, 2001), requires Federal agencies to prepare and submit to OMB, a Statement of Energy Effects for any significant energy action. A ''significant energy action'' is defined as any action by an agency that promulgated or is expected to lead to promulgation of a final rule, and that (1) is a significant regulatory action under Executive Order 12866, or any successor order; and (2) is likely to have a significant adverse effect on the supply, distribution, or use of energy; or (3) is designated by the Administrator of OIRA as a significant energy action. For any significant energy action, the agency must give a detailed statement of any adverse effects on energy supply, distribution, or use if the regulation is implemented, and of reasonable alternatives to the action and their expected benefits on energy supply, distribution, and use.

This regulatory action is not a significant regulatory action under Executive Order 12866. Moreover, it would not have a significant adverse effect on the supply, distribution, or use of energy, nor has it been designated as a significant energy action by the Administrator of OIRA. Therefore, it is not a significant energy action, and, accordingly, DOE has not prepared a Statement of Energy Effects.

M. Review Under Section 32 of the Federal Energy Administration Act of 1974

Under section 301 of the Department of Energy Organization Act (Pub. L. 95–91; 42 U.S.C. 7101), DOE must comply with section 32 of the Federal Energy Administration Act of 1974, as amended by the Federal Energy Administration Authorization Act of 1977. (15 U.S.C. 788; ''FEAA'') Section 32 essentially provides in relevant part that, where a proposed rule authorizes or requires use of commercial standards, the notice of proposed rulemaking must inform the public of the use and background of such standards. In addition, section 32(c) requires DOE to consult with the Attorney General and the Chairman of the Federal Trade Commission (''FTC'') concerning the impact of the commercial or industry standards on competition.

The modifications to the test procedure for fluorescent lamp ballasts adopted in this final rule incorporates testing methods contained in the following commercial standards:

(1) ANSI Standard C78.901, ''American National Standard for Electric Lamps—Single-Based Fluorescent Lamps—Dimensional and Electrical Characteristics,'' 2016;

(2) ANSI C78.81–2016, ''American National Standard for Electric Lamps—Double-Capped Fluorescent Lamps—Dimensional and Electrical Characteristics,'' 2016;

(3) ANSI C78.375A, ''American National Standard for Electric Lamps—Fluorescent Lamps—Guide for Electrical Measures,'' 2014;

(4) ANSI Standard C82.11–2017, ''American National Standard for Lamp Ballasts—High Frequency Fluorescent Lamp Ballasts—Supplements,'' 2017;

(5) ANSI Standard C82.77, ''American National Standard for Lighting Equipment—Harmonic Emission Limits—Related Power Quality Requirements for Lighting Equipment,'' 2002;

(6) ANSI Standard C82.1, ''American National Standard for Lamp Ballasts—Line Frequency Fluorescent Lamp Ballast,'' 2015;

(7) ANSI Standard C82.2, ''American National Standard for Lamp Ballasts—Method of Measurement of Fluorescent Lamp Ballasts,'' 2016;

(8) ANSI Standard C82.3, (''ANSI C82.3'') ''American National Standard for Lamp Ballasts—Reference Ballasts for Fluorescent Lamps,'' approved April 8, 2016.

99) IEC Standard 60081, ''Double Capped Fluorescent Lamps—Performance specifications (Amendment 6, Edition 5.0, August 2017),'' 2013; and

(10) IEC Standard 62301, ''Household electrical appliances—Measurement of standby power (Edition 2.0, January 2011),'' 2011.

DOE has evaluated these standards and is unable to conclude whether they fully comply with the requirements of section 32(b) of the FEAA (*i.e.,* whether they were developed in a manner that fully provides for public participation, comment, and review.) DOE has consulted with both the Attorney General and the Chairman of the FTC about the impact on competition of using the methods contained in these standards and has received no comments objecting to their use.

N. Congressional Notification

As required by 5 U.S.C. 801, DOE will report to Congress on the promulgation of this rule before its effective date. The report will state that it has been determined that this rule is not a ''major rule'' as defined by 5 U.S.C. 804(2).

O. Description of Materials Incorporated by Reference

In this final rule, DOE incorporates by reference the test standard published by ANSI, titled ''American National Standard for Electric Lamps—Single-Based Fluorescent Lamps—Dimensional and Electrical Characteristics,'' ANSI/NEMA C78.901–2016. ANSI C78.901–2016 is an industry accepted test standard that describes physical and electrical characteristics of single-based fluorescent lamps. The test procedure adopted in this final rule references sections of ANSI C78.901–2016 for characteristics of reference lamps that must be used when testing fluorescent lamp ballasts. ANSI C78.901–2016 is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference the test standard published by ANSI, titled ''American National Standard for Electric Lamps—Double-Capped Fluorescent Lamps—Dimensional and Electrical Characteristics,'' ANSI C78.81–2016. ANSI C78.81–2016 is an industry accepted test standard that describes the physical and electrical characteristics of double-capped fluorescent lamps. The test procedure adopted in this final rule references sections of ANSI C78.81–2016 for characteristics of reference lamps that must be used when testing fluorescent lamp ballasts. ANSI C78.81–2016 is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference the test standard published by ANSI, titled ''American National Standard for Electric Lamps—Fluorescent Lamps—Guide for Electrical Measures,'' ANSI C78.375A–2014. ANSI C78.375A–2014 is an industry accepted test standard that describes procedures for measuring the electrical characteristics of fluorescent lamps. The test procedure adopted in this final rule references sections of ANSI C78.375A–2014 for testing performance of fluorescent lamp ballasts. ANSI C78.375A–2014 is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference the test standard published by ANSI, titled ''American National Standard for Lamp Ballasts—High Frequency Fluorescent Lamp Ballasts—Supplements,'' ANSI/NEMA C82.11–2017. ANSI/NEMA C82.11–2017 is an industry accepted test standard that describes characteristics and measurements of high frequency fluorescent lamp ballasts. The test procedure adopted in this final rule references sections of ANSI/NEMA C82.11–2017 for testing performance of fluorescent lamp ballasts. ANSI/NEMA C82.11–2017 is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE maintains the incorporation by reference of the test standard published by ANSI, titled ''American National Standard for Lamp Ballasts—Definitions for Fluorescent Lamps and Ballasts,'' ANSI C82.13–2002. ANSI C82.13–2002 is an industry accepted standard that that provides definitions for terms used in ANSI C78 and ANSI C82 series standards for fluorescent lamps and ballasts. ANSI C82.13–2002, incorporated by reference provides definitions for terms used in the DOE test procedure for fluorescent lamp ballasts. ANSI C82.13–2002 is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference sections of the test standard published by ANSI, titled ''American National Standard Harmonic Emission Limits—Related Power Quality Requirements for Lighting Equipment,'' ANSI C82.77–2002. ANSI C82.77–2002 is an industry accepted standard that describes maximum harmonic emission limits for lighting equipment. ANSI/NEMA C82.11–2017, incorporated by reference in this final rule for testing high frequency fluorescent lamp ballasts, references ANSI C82.77–2002 to determine the maximum harmonic emission limits of the input current to the ballast. ANSI C82.77–2002 is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference the test standard published by ANSI, titled ''American National Standard for Lamp Ballasts—Line Frequency Fluorescent Lamp Ballast,'' ANSI C82.1–2004 (R2008, R2015). ANSI C82.1–2004 (R2008, R2015) (also referred to in this rulemaking as ''ANSI C82.1–2015'') is an industry accepted test standard that describes characteristics and measurements of line frequency fluorescent lamp ballasts. The test procedure adopted in this final rule references ANSI C82.1–2004 (R2008, R2015) for testing performance of fluorescent lamp ballasts. ANSI C82.1–2004 (R2008, R2015) is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference the test standard published by ANSI, titled ''American National Standard for Lamp Ballasts—Method of Measurement of Fluorescent Lamp Ballasts,'' ANSI C82.2–2002 (R2007, R2016). ANSI C82.2–2002 (R2007, R2016) (also referred to in this rulemaking as ANSI C82.2–2016) is an industry accepted standard for testing line frequency fluorescent lamp ballasts. The 2016 version is a reaffirmation of the 2002 version. ANSI C82.2–2002 (R2007, R2016) is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference the test standard published by ANSI, titled ''American National Standard for Lamp Ballasts—Reference Ballasts for Fluorescent Lamps,'' ANSI C82.3–2016. ANSI C82.3–2016 (also referred to in this rulemaking as ANSI C82.3) is an industry accepted standard that describes characteristics and requirements of fluorescent lamp reference ballasts. The test procedure adopted in this final rule references ANSI C82.3–2016 for determining a reference fluorescent lamp to use when testing the performance of fluorescent lamp ballasts. ANSI C82.3–2016 is readily available on ANSI's website at *http://webstore.ansi.org/.*

In this final rule, DOE incorporates by reference the test standard published by IEC, titled, ''Double Capped Fluorescent Lamps—Performance specifications (IEC 60081:1997/AMD6, Amendment 6, Edition 5.0, August 2017),'' IEC 60081 Amendment 6. IEC 60081 Amendment 6 is an industry accepted test standard that describes physical and electrical characteristics of double-capped fluorescent lamps. The test procedure adopted in this final rule reference sections of IEC 60081 Amendment 6 for characteristics of reference lamps that must be used when testing fluorescent lamp ballasts. IEC 60081 Amendment 6 is readily available on IEC's website at *https://webstore.iec.ch/home.*

In this final rule, DOE incorporates by reference the test standard published by IEC, titled ''Household electrical appliances—Measurement of standby power (Edition 2.0, January 2011),'' IEC 62301 (Edition 2.0). IEC 62301 (Edition 2.0) is an industry accepted test standard that describes measurements of electrical power consumption in standby mode, off mode, and network mode. The test procedure adopted in this final rule reference sections of IEC 62301 (Edition 2.0) for testing standby mode power consumption of fluorescent lamp ballasts. IEC 62301 (Edition 2.0) is readily available on IEC's website at *https://webstore.iec.ch/home.*

V. Approval of the Office of the Secretary

The Secretary of Energy has approved publication of this final rule.

List of Subjects

10 CFR Part 429

Administrative practice and procedure, Confidential business information, Energy conservation, Household appliances, Reporting and recordkeeping requirements.

10 CFR Part 430

Administrative practice and procedure, Confidential business information, Energy conservation, Household appliances, Imports, Incorporation by reference, Intergovernmental relations, Small businesses.

Signing Authority

This document of the Department of Energy was signed on July 1, 2020, by Alexander N. Fitzsimmons, Deputy Assistant Secretary for Energy Efficiency, Energy Efficiency and Renewable Energy, pursuant to delegated authority from the Secretary of Energy. That document with the original signature and date is maintained by DOE. For administrative purposes only, and in compliance with requirements of the Office of the Federal Register, the undersigned DOE Federal Register Liaison Officer has been authorized to sign and submit the document in electronic format for publication, as an official document of the Department of Energy. This administrative process in no way alters the legal effect of this document upon publication in the **Federal Register**.

Signed in Washington, DC, on July 2, 2020.

Treena V. Garrett,

Federal Register Liaison Officer, U.S. Department of Energy.

For the reasons stated in the preamble, DOE amends parts 429 and 430 of chapter II of title 10, Code of Federal Regulations as set forth below:

PART 429—CERTIFICATION, COMPLIANCE, AND ENFORCEMENT FOR CONSUMER PRODUCTS AND COMMERCIAL AND INDUSTRIAL EQUIPMENT

■ 1. The authority citation for part 429 continues to read as follows:

Authority: 42 U.S.C. 6291–6317; 28 U.S.C. 2461 note.

■ 2. Section 429.26 is amended by:

■ a. Revising the introductory text of paragraph (a)(2)(i);

■ b. Adding paragraph (a)(2)(iii); and

■ c. Revising paragraphs (b)(2) and (c).

The revisions and addition read as follows:

§ 429.26 Fluorescent lamp ballasts.

(a) * * *

(2) * * *

(i) Any represented value of the energy consumption of a basic model for which consumers would favor lower values shall be greater than or equal to the higher of:

* * * * *

(iii) The represented value of average total lamp arc power must be equal to the mean of the sample,

$$\bar{x} = \frac{1}{n}\sum_{i=1}^{n} x_i$$

Where:

$\bar{x}$ is the sample mean;
n is the number of units in the sample; and
x_i is the i^{th} unit.

(b) * * *

(2) Pursuant to § 429.12(b)(13), a certification report must include the following public product-specific information: The ballast luminous efficiency, the average total lamp arc power, the power factor, the number of lamps operated by the ballast, and the type of lamps operated by the ballast (*i.e.,* wattage, base, shape, diameter, and length).

(c) *Rounding requirements.* (1) Round ballast luminous efficiency to the nearest thousandths place.

(2) Round power factor to the nearest hundredths place.

(3) Round average total lamp arc power to the nearest tenth of a watt.

PART 430—ENERGY CONSERVATION PROGRAM FOR CONSUMER PRODUCTS

■ 3. The authority citation for part 430 continues to read as follows:

Authority: 42 U.S.C.6291–6309; 28 U.S.C. 2461 note.

■ 4. Section 430.2 is amended by revising the definition of ''Designed and marketed'' to read as follows:

§ 430.2 Definitions.

* * * * *

Designed and marketed means that the intended application of the lamp or ballast is clearly stated in all publicly available documents (*e.g.,* product literature, catalogs, and packaging labels). This definition is applicable to terms related to the following covered lighting products: Fluorescent lamp ballasts; fluorescent lamps; general service fluorescent lamps; general service incandescent lamps; general service lamps; incandescent lamps; incandescent reflector lamps; medium base compact fluorescent lamps; and specialty application mercury vapor lamp ballasts.

* * * * *

■ 5. Section 430.3 is amended by:

■ a. Revising paragraph (a);

■ b. Removing the references ''§ 430.2, § 430.32, appendix Q,'' and adding in their place ''§§ 430.2 and 430.32'' in paragraph (e)(5);

■ c. Removing the words ''appendix Q and'' in paragraph (e)(6);

■ d. Removing the words '', appendix Q,'' in paragraph (e)(7);

■ e. Redesignating paragraphs (e)(17) through (21) as (e)(22) through (26);

■ f. Redesignating paragraphs (e)(6) through (16) as follows:

Old paragraph	New paragraph
(e)(6)	(e)(7)
(e)(7)	(e)(9)
(e)(8)	(e)(10)
(e)(9)	(e)(12)
(e)(10)	(e)(13)
(e)(11)	(e)(14)
(e)(12)	(e)(15)
(e)(13)	(e)(16)
(e)(14)	(e)(17)
(e)(15)	(e)(19)
(e)(16)	(e)(20)

■ g. Adding new paragraphs (e)(6), (8), and (11);

■ h. Revising newly redesignated paragraphs (e)(15) and (16);

■ i. Removing the words ''appendix Q and'' in newly redesignated paragraph (e)(17);

■ j. Adding new paragraph (e)(18);

■ k. Revising newly redesignated paragraph (e)(19);

■ l. Adding new paragraph (e)(21);

■ m. Adding Note 1 to paragraph (e);

■ n. Revising paragraph (o)(2); and

■ o. Removing the references ''appendices C1, D1, D2, G, H, I, J2, N, O, P, X, X1, Y, Z, BB, and CC to subpart B'' in paragraph (o)(6) and adding in their place the references ''appendices C1, D1, D2, G, H, I, J2, N, O, P, Q, X, X1, Y, Z, BB, and CC to subpart B''.

The revisions and additions read as follows:

§ 430.3 Materials incorporated by reference.

(a) *General.* We incorporate by reference the following standards into this part. The material listed has been approved for incorporation by reference by the Director of the Federal Register in accordance with 5 U.S.C. 552(a) and 1 CFR part 51. To enforce any edition other than that specified in this section, the Department of Energy must publish a document in the **Federal Register** and the material must be available to the public. All approved material is available for inspection at U.S. Department of Energy, Office of Energy Efficiency and Renewable Energy, Building Technologies Program, 6th Floor, 950 L'Enfant Plaza, SW, Washington, DC 20024, (202) 586–2945, or go to: *www1.eere.energy.gov/buildings/appliance__standards/.* Standards can be obtained from the sources listed in this section. Material is also available for inspection at the National Archives and Records Administration (NARA). For information on the availability of this material at NARA, email *fedreg.legal@nara.gov,* or go to: *www.archives.gov/federal-register/cfr/ibr-locations.html.*

* * * * *

(e) * * *

(6) ANSI C78.81–2016, (''ANSI C78.81–2016''), American National Standard for Electric Lamps—Double-Capped Fluorescent Lamps—Dimensional and Electrical Characteristics, approved June 29, 2016, IBR approved for appendix Q to subpart B.

* * * * *

(8) ANSI C78.375A–2014, (''ANSI C78.375A''), American National Standard for Electric Lamps—Fluorescent Lamps—Guide for Electrical Measures, approved August 28, 2014, IBR approved for appendix Q to subpart B.

* * * * *

(11) ANSI/NEMA C78.901–2016 (''ANSI C78.901–2016''), American National Standard for Electric Lamps—Single-Based Fluorescent Lamps—Dimensional and Electrical Characteristics, ANSI approved August 23, 2016, IBR approved for appendix Q to subpart B.

* * * * *

(15) ANSI C82.1–2004 (R2008, R2015), (''ANSI C82.1''), American National Standard for Lamp Ballasts—Line Frequency Fluorescent Lamp Ballasts, approved November 20, 2015; IBR approved for appendix Q to subpart B.

(16) ANSI C82.2–2002 (R2007, R2016), (''ANSI C82.2''), American National Standard for Lamp Ballasts—Method of Measurement of Fluorescent Lamp Ballasts, approved July 12, 2016, IBR approved for appendix Q to subpart B.

* * * * *

(18) ANSI C82.3–2016, (''ANSI C82.3''), American National Standard for Reference Ballasts for Fluorescent Lamps, approved April 8, 2016; IBR approved for appendix Q to subpart B.

(19) ANSI/NEMA C82.11–2017, (''ANSI C82.11''), American National Standard for Lamp Ballasts—High-Frequency Fluorescent Lamp Ballasts, approved January 23, 2017; IBR approved for appendix Q to subpart B.

* * * * *

(21) ANSI C82.77–2002, (''ANSI C82.77'') Harmonic Emission Limits—Related Power Quality Requirements for Lighting Equipment, approved January 17, 2002; IBR approved for appendix Q to subpart B.

* * * * *

Note 1 to paragraph (e). The standards referenced in paragraphs (e)(6), (8), (11), (15), (16), (18), (19), and (21) of this section were all published by National Electrical Manufacturers Association (NEMA) and are also available from National Electrical Manufacturers Association, 1300 North 17th Street, Suite 900, Rosslyn, Virginia 22209, *https://www.nema.org/Standards/Pages/default.aspx.*

* * * * *

(o) * * *

(2) IEC 60081:1997/AMD6, (''IEC 60081''), Double-capped fluorescent lamps—Performance specifications (Amendment 6, Edition 5.0, August 2017); IBR approved for appendix Q to subpart B.

* * * * *

■ 6. Section 430.23 is amended by revising paragraph (q) to read as follows:

§ 430.23 Test procedures for the measurement of energy and water consumption.

* * * * *

(q) *Fluorescent lamp ballasts.* (1) Calculate ballast luminous efficiency (BLE) using appendix Q to this subpart.

(2) Calculate power factor using appendix Q to this subpart.

* * * * *

■ 7. Appendix Q to subpart B of part 430 is revised to read as follows:

Appendix Q to Subpart B of Part 430—Uniform Test Method for Measuring the Energy Consumption of Fluorescent Lamp Ballasts

Note regarding effective date: After October 14, 2020 and prior to March 15, 2021 any representations with respect to energy use or efficiency of fluorescent lamp ballasts must be in accordance with the results of testing pursuant to this appendix or the test procedures as they appeared in appendix Q to this subpart revised as of January 1, 2020. On or after March 15, 2021, any representations, including certifications of compliance for ballasts subject to any energy conservation standard, made with respect to the energy use or efficiency of fluorescent lamp ballasts must be made in accordance with the results of testing pursuant to this appendix.

0. Incorporation by Reference

DOE incorporated by reference ANSI C78.81–2016, ANSI C78.375A, ANSI C78.901–2016, ANSI C82.1, ANSI 82.2, ANSI 82.3, ANSI 82.11, ANSI C82.13, ANSI 82.77, IEC 60081, and IEC 62301, each in their entirety in § 430.3; however, only enumerated provisions of ANSI C78.375A, ANSI C82.2, and IEC 62301 are applicable to this appendix, as follows:

(a) ANSI C78.375A, as follows:

(i) Section 4, Ambient conditions for temperature measurement, as specified in section 2.4.2 of this appendix; and

(ii) Section 9, Electrical instruments, as specified in sections 2.2.1, 2.2.2, and 2.2.3 of this appendix.

(b) ANSI C82.2, as follows:

(i) Section 3, Pertinent measurements, as specified in section 2.4.1 of this appendix;

(ii) Section 4, Electrical supply characteristics—test ballast measurement circuits, as specified in section 2.4.1 of this appendix; and

(iii) Section 7, Test measurements circuits, as specified in sections 2.5.6, 2.5.7, and 2.5.8 of this appendix.

(c) IEC 62301 as follows:

(i) Section 5, Measurements, as specified in sections 3.4.3 and 3.4.4 of this appendix.

1. Definitions

1.1. *Average total lamp arc power* means the sample mean of the total lamp arc power of the ballast units tested.

1.2. *Dimming ballast* means a ballast that is designed and marketed to vary its output and that can achieve an output less than or equal to 50 percent of its maximum electrical output.

1.3. *High frequency ballast* is as defined in ANSI C82.13 (incorporated by reference; see § 430.3).

1.4. *Instant-start* is the starting method used in instant-start systems as defined in ANSI C82.13, as typically indicated on publicly available documents of a fluorescent lamp ballast (*e.g.,* product literature, catalogs, and packaging labels).

1.5. *Low-frequency ballast* is a fluorescent lamp ballast that operates at a supply frequency of 50 to 60 Hz and operates the lamp at the same frequency as the supply.

1.6. *Programmed-start* is the starting method used in a programmed-start system as defined in ANSI C82.13, as typically indicated on publicly available documents of a fluorescent lamp ballast (*e.g.,* product literature, catalogs, and packaging labels).

1.7. *Rapid-start* is the starting method used in rapid-start type systems as defined in ANSI C82.13, as typically indicated on publicly available documents of a fluorescent lamp ballast (*e.g.,* product literature, catalogs, and packaging labels).

1.8. *Reference lamp* is a fluorescent lamp that meets the operating conditions of a reference lamp as defined by ANSI C82.13.

1.9. *Residential ballast* means a fluorescent lamp ballast that meets Federal Communications Commission (FCC) consumer limits as set forth in 47 CFR part

18 and is designed and marketed for use only in residential applications.

1.10. *RMS* is the root mean square of a varying quantity.

1.11 *Sign Ballast* means a ballast that has an Underwriters Laboratories Inc. Type 2 rating and is designed and marketed for use only in outdoor signs.

2. Active Mode Procedure for Measuring BLE at Full Light Output

2.1. Where ANSI C82.2 (incorporated by reference; see § 430.3) references ANSI C82.1, use ANSI C82.1 (incorporated by reference; see § 430.3) for testing low-frequency ballasts and use ANSI C82.11 (incorporated by reference; see § 430.3) for testing high-frequency ballasts. In addition when applying ANSI C82.2, use the standards ANSI C78.375A, ANSI C78.81–2016, ANSI C82.1, ANSI C82.11, ANSI C82.13, ANSI C82.3, ANSI C82.77, and ANSI C78.901–2016 (incorporated by reference; see § 430.3) instead of the normative references in ANSI 82.2. Specifications in referenced standards that are recommended, that ''shall'' or ''should'' be met, or that are not clearly mandatory, are mandatory. In cases where there is a conflict between any industry standard(s) and this appendix, the language of the test procedure in this appendix takes precedence over the industry standard(s).

2.2. Instruments

2.2.1. All instruments must meet the specifications of section 9 of ANSI C78.375A.

2.2.2. *Power Analyzer.* In addition to the specifications in section 9 of ANSI C78.375A, the power analyzer must have a maximum 100 pF capacitance to ground and frequency response between 40 Hz and 1 MHz.

2.2.3. *Current Probe.* In addition to the specifications in section 9 of ANSI C78.375A, the current probe must be galvanically isolated and have frequency response between 40 Hz and 20 MHz.

2.3. Test Setup

2.3.1. Connect the ballast to a main power source and to the fluorescent lamp(s) as specified in this section. Ensure the ballast is connected to fluorescent lamp(s) according to any manufacturer's wiring instructions on or sold with each unit (including those provided online). To test a low-frequency ballast, follow ANSI C82.1 but disregard section 5.3 of ANSI C82.1. To test a high-frequency ballast, follow ANSI C82.11 but disregard sections 5.3.1 and 5.13 and Annex D of ANSI C82.11.

2.3.2. In the test setup, all wires used in the apparatus, including any wires from the ballast to the lamps and from the lamps to the measuring devices, must meet the following specifications:

2.3.2.1. Use the wires provided by the ballast manufacturer and only the minimum wire length necessary to reach both ends of each lamp. If the wire lengths supplied with the ballast are too short to reach both ends of each lamp, add the minimum additional wire length necessary to reach both ends of each lamp, using wire of the same wire gauge(s) as the wire supplied with the ballast. If no wiring is provided with the ballast, use 18 gauge or thicker wire.

2.3.2.2. Keep wires loose. Do not shorten or allow bundling of any wires. Separate all wires from each other, and ground them to prevent parasitic capacitance.

2.3.3. Test each ballast with only one fluorescent lamp type. Select the one type of fluorescent lamp for testing as follows:

2.3.3.1. Each fluorescent lamp must meet the specifications of a reference lamp as defined by ANSI C82.13, be seasoned at least 12 hours, and be stabilized as specified in 2.5.2.1 of this appendix. Test each reference lamp with a reference ballast that meets the criteria of ANSI C82.3. For low frequency ballasts that operate:

(a) 32 W 4-foot medium bipin T8 lamps, use the following reference lamp specifications: 30.8 W, arc wattage; 1.7 W, approximate cathode wattage (with 3.6 V on each cathode); 32.5 W, total wattage; 137 V, voltage; 0.265 A, current. Test the selected reference lamp with the following reference ballast specifications: 300 V, rated input voltage; 0.265 A, reference current; 910 ohms, impedance. Use the following cathode heat requirements for rapid start: 3.6 V nominal, voltage; 2.5 V min, 4.4 V max, limits during operation; 11.0 ohms +/− 0.1 ohms, dummy load resistor; 3.4 V min, 4.5 V max, voltage across dummy load.

(b) 59 W 8-foot single pin T8 lamps, use the following reference lamp specifications: 60.1 W, arc wattage; 270.3 V, voltage; 0.262 A, current. Test the selected reference lamp with the following reference ballast specifications: 625 V, rated input voltage; 0.260 A, reference current; 1960 ohms, impedance.

(c) 32 W 2-foot U-shaped medium bipin T8 lamps, use the following reference lamp specifications: 30.5 W, arc wattage; 1.7 W, approximate cathode wattage (with 3.6 V on each cathode); 32.2 W, total wattage; 137 V, voltage; 0.265 A, current. Test the selected reference lamp with the following reference ballast specifications: 300 V, rated input voltage; 0.265 A, reference current; 910 ohms, impedance. Use the following cathode heat requirements for rapid start: 3.6 V nominal, voltage; 2.5 V min, 4.4 V max, limits during operation; 11.0 ohms +/- 0.1 ohms, dummy load resistor; 3.4 V min, 4.5 V max, voltage across dummy load.

2.3.3.2 For any sign ballast designed and marketed to operate both T8 and T12 lamps, use a T12 lamp as specified in Table 1 of this appendix.

2.3.3.3. For any ballast designed and marketed to operate lamps of multiple base types, select lamp(s) of one base type, in the following order of decreasing preference: Medium bipin, miniature bipin, single pin, or recessed double contact.

2.3.3.4. After selecting the base type (per section 2.3.3.3), select the diameter of the reference lamp. Any ballast designed and marketed to operate lamps of multiple diameters, except for any sign ballast capable of operating both T8 and T12 lamps, must be tested with lamps of one of those diameters, selected in the following order of decreasing preference: T8, T5, or T12.

2.3.3.5. Connect the ballast to the maximum number of lamps (lamp type as determined by 2.3.3.2, 2.3.3.3, and 2.3.3.4 of this section) the ballast is designed and marketed to operate simultaneously.

For any ballast designed and marketed to operate both 4-foot medium bipin lamps and 2-foot U-shaped lamps, test with the maximum number of 4-foot medium bipin lamp(s).

2.3.3.6. Test each ballast with the lamp type specified in Table A of this section that corresponds to the lamp diameter and base type the ballast is designed and marketed to operate.

TABLE 1 TO SECTION 2.3.3.6—LAMP-AND-BALLAST PAIRINGS AND FREQUENCY ADJUSTMENT FACTORS

Ballast type	Lamp type: Lamp diameter and base	Lamp type: Nominal lamp wattage	Frequency adjustment factor (β): Low-frequency	Frequency adjustment factor (β): High-frequency
Ballasts that operate straight-shaped lamps (commonly referred to as 4-foot medium bipin lamps) with medium bipin bases and a nominal overall length of 48 inches.	T8 MBP (Data Sheet 7881–ANSI–1005–4) *.	32	0.94	1.0
	T12 MBP (Data Sheet 7881–ANSI–1006–1) *.	34	0.93	1.0
Ballasts that operate U-shaped lamps (commonly referred to as 2-foot U-shaped lamps) with medium bipin bases and a nominal overall length between 22 and 25 inches.	T8 MBP (Data Sheet 78901–ANSI–4027–2) *.	32	0.94	1.0
	T12 MBP **	34	0.93	1.0
Ballasts that operate lamps (commonly referred to as 8-foot-high output lamps) with recessed double contact bases and a nominal overall length of 96 inches.	T8 HO RDC (Data Sheet 7881–ANSI–1501–2) *.	86	0.92	1.0
	T12 HO RDC (Data Sheet 7881–ANSI–1017–1) *.	95	0.94	1.0

TABLE 1 TO SECTION 2.3.3.6—LAMP-AND-BALLAST PAIRINGS AND FREQUENCY ADJUSTMENT FACTORS—Continued

Ballast type	Lamp type		Frequency adjustment factor (β)	
	Lamp diameter and base	Nominal lamp wattage	Low-frequency	High-frequency
Ballasts that operate lamps (commonly referred to as 8-foot slimline lamps) with single pin bases and a nominal overall length of 96 inches.	T8 slimline SP (Data Sheet 7881–ANSI–1505–1) *. T12 slimline SP (Data Sheet 7881–ANSI–3006–1) *.	59 60	0.95 0.94	1.0 1.0
Ballasts that operate straight-shaped lamps (commonly referred to as 4-foot miniature bipin standard output lamps) with miniature bipin bases and a nominal length between 45 and 48 inches.	T5 SO Mini-BP (Data Sheet 60081–IEC–6640–7) *.	28	0.95	1.0
Ballasts that operate straight-shaped lamps (commonly referred to as 4-foot miniature bipin high output lamps) with miniature bipin bases and a nominal length between 45 and 48 inches.	T5 HO Mini-BP (Data Sheet 60081–IEC–6840–6) *.	54	0.95	1.0
Sign ballasts that operate lamps (commonly referred to as 8-foot high output lamps) with recessed double contact bases and a nominal overall length of 96 inches.	T8 HO RDC (Data Sheet 7881–ANSI–1501–2) *. T12 HO RDC (Data Sheet 7881–ANSI–1019–1) *.	86 † 110	0.92 0.94	1.0 1.0

MBP, Mini-BP, RDC, and SP represent medium bipin, miniature bipin, recessed double contact, and single pin, respectively.

* Data Sheet corresponds to ANSI C78.81–2016, ANSI C78.901–2016, or IEC 60081 page number (incorporated by reference; see § 430.3).

** No ANSI or IEC Data Sheet exists for 34 W T12 MBP U-shaped lamps. For ballasts designed and marketed to operate only T12 2-foot U-shaped lamps with MBP bases and a nominal overall length between 22 and 25 inches, select T12 U-shaped lamps designed and marketed as having a nominal wattage of 34 W.

† This lamp type is commonly marketed as 110 W; however, the ANSI C78.81–2016 Data Sheet (incorporated by reference; see § 430.3) lists nominal wattage of 113 W. Test with specifications for operation at 0.800 amperes (A).

2.3.4. Test Circuits

2.3.4.1. The power analyzer test setup must have exactly n + 1 channels, where n is the maximum number of lamps (lamp type as determined by sections 2.3.3.2, 2.3.3.3, and 2.3.3.4 of this appendix) a ballast is designed and marketed to operate. Use the minimum number of power analyzers possible during testing. Synchronize all power analyzers. A system may be used to synchronize the power analyzers.

2.3.4.2. *Lamp Arc Voltage.* Attach leads from the power analyzer to each fluorescent lamp according to Figure 1 of this section for rapid- and programmed-start ballasts; Figure 2 of this section for instant-start ballasts operating single pin (SP) lamps; and Figure 3 of this section for instant-start ballasts operating medium bipin (MBP), miniature bipin (mini-BP), or recessed double contact (RDC) lamps. The programmed- and rapid-start ballast test setup includes two 1000 ohm resistors placed in parallel with the lamp pins to create a midpoint from which to measure lamp arc voltage.

2.3.4.3. *Lamp Arc Current.* Position a current probe on each fluorescent lamp according to Figure 1 of this section for rapid- and programmed-start ballasts; Figure 2 of this section for instant-start ballasts operating SP lamps; and Figure 3 of this section for instant-start ballasts operating MBP, mini-BP, and RDC lamps.

For the lamp arc current measurement, set the full transducer ratio in the power analyzer to match the current probe to the power analyzer.

$$Full\ Transducer\ Ratio = \frac{I_{in}}{V_{out}} \times \frac{R_{in}}{R_{in} + R_s}$$

Where: I_{in} is the current through the current transducer, V_{out} is the voltage out of the transducer, R_{in} is the power analyzer impedance, and R_s is the current probe output impedance.

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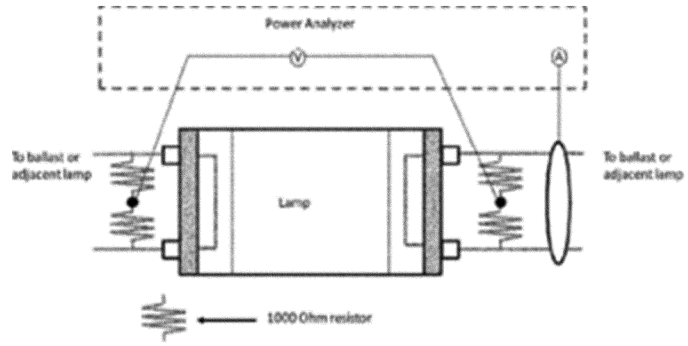

Figure 1: Programmed- and Rapid-Start Ballast Instrumentation Setup

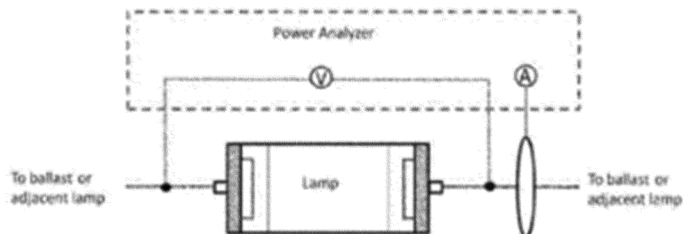

Figure 2: Instant-Start Ballasts that Operate SP Lamps Instrumentation Setup

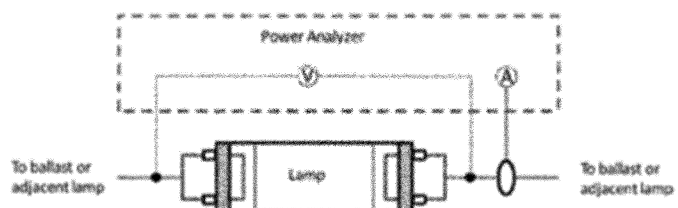

Figure 3: Instant-Start Ballasts that Operate MBP, mini-BP, and RDC Lamps Instrumentation Setup

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2.4. Test Conditions

2.4.1. Establish and maintain test conditions for testing fluorescent lamp ballasts in accordance with sections 3 and 4 of ANSI C82.2.

2.4.2. *Room Temperature and Air Circulation.* Maintain the test area at 25 ±1 °C, with minimal air movement as defined in section 4 of ANSI C78.375A.

2.4.3. *Input Voltage.* For any ballast designed and marketed for operation at only one input voltage, test at that specified voltage. For any ballast that is neither a residential ballast nor a sign ballast but is designed and marketed for operation at multiple voltages, test the ballast at 277 V ±0.1%. For any residential ballast or sign ballast designed and marketed for operation at multiple voltages, test the ballast at 120 V ±0.1%.

2.5. Test Method

2.5.1. Connect the ballast to the selected fluorescent lamps (as determined in section 2.3.3 of this appendix) and to measurement instrumentation as specified in the Test Setup in section 2.3 of this appendix.

2.5.2. Determine stable operating conditions according to Option 1 or Option 2.

2.5.2.1. Option 1. Operate the ballast for at least 15 minutes before determining stable operating conditions. Determine stable operating conditions by measuring lamp arc voltage, current, and power once per minute in accordance with the setup described in section 2.3 of this appendix. The system is stable once the difference between the maximum and minimum for each value of lamp arc voltage, current, and power divided by the average value of the measurements do not exceed one percent over a four minute moving window. Once stable operating conditions are reached, measure each of the parameters described in sections 2.5.3 through 2.5.9 of this appendix.

2.5.2.2 Option 2. Determine stable operating conditions for lamp arc voltage, current, and power according to steps 1 through 6 of section D.2.1 in Annex D of ANSI C82.11.

2.5.3. *Lamp Arc Voltage.* Measure lamp arc voltage in volts (RMS) using the setup in section 2.3.4.2.

2.5.4. *Lamp Arc Current.* Measure lamp arc current in amps (RMS) using the setup in section 2.3.4.3 of this appendix.

2.5.5. *Lamp Arc Power.* The power analyzer must calculate output power by using the measurements from sections 2.5.3 and 2.5.4 of this appendix.

2.5.6. *Input Power.* Measure the input power in watts to the ballast in accordance with section 7 of ANSI C82.2 (disregard references to Figure 1 and Figure 3).

2.5.7. *Input Voltage.* Measure the input voltage in volts (RMS) to the ballast in accordance with section 7 of ANSI C82.2 (disregard references to Figure 1 and Figure 3).

2.5.8. *Input Current.* Measure the input current in amps (RMS) to the ballast in accordance with section 7 of ANSI C82.2 (disregard references to Figure 1 and Figure 3).

2.5.9. *Lamp Operating Frequency.* Measure the frequency of the waveform delivered from the ballast to any lamp used in the test in accordance with the setup in section 2.3 of this appendix.

2.6. Calculations

2.6.1. Calculate ballast luminous efficiency (BLE) as follows (do not round values of total lamp arc power and input power prior to calculation):

$$Ballast\ Luminous\ Efficiency = \frac{Total\ Lamp\ Arc\ Power}{Input\ Power} \times \beta$$

Where: Total Lamp Arc Power is the sum of the lamp arc powers for all lamps operated by the ballast as measured in section 2.5.5 of this appendix, Input Power is as determined by section 2.5.6 of this appendix, and β is equal to the frequency adjustment factor in Table 1 of this appendix.

2.6.2. Calculate Power Factor (PF) as follows (do not round values of input power, input voltage, and input current prior to calculation):

$$PF = \frac{Input\ Power}{Input\ Voltage\ \times Input\ Current}$$

Where: Input Power is measured in accordance with section 2.5.6 of this appendix, Input Voltage is measured in accordance with section 2.5.7 of this appendix, and Input Current is measured in accordance with section 2.5.8 of this appendix.

3. Standby Mode Procedure

3.1. The measurement of standby mode power is required to be performed only if a manufacturer makes any representations with respect to the standby mode power use of the fluorescent lamp ballast. When there is a conflict, the language of the test procedure in this appendix takes precedence over IEC 62301 (incorporated by reference; see § 430.3). Specifications in referenced standards that are not clearly mandatory are mandatory. Manufacturer's instructions, such as ''instructions for use'' referenced in IEC 62301 mean the manufacturer's instructions that come packaged with or appear on the unit, including on a label. It may include an online manual if specifically referenced (*e.g.,* by date or version number) either on a label or in the packaged instructions. Instructions that appear on the unit take precedence over instructions available electronically, such as through the internet.

3.2. Test Setup

3.2.1. Take all measurements with instruments as specified in section 2.2 of this appendix. Fluorescent lamp ballasts that are designed and marketed for connection to control devices must be tested with all commercially available compatible control devices connected in all possible configurations. For each configuration, a separate measurement of standby power must be made in accordance with section 3.4 of this appendix.

3.2.2. Connect each ballast to the maximum number of lamp(s) as specified in section 2.3 (specifications in 2.3.3.1 are optional) of this appendix. Note: ballast operation with reference lamp(s) is not required.

3.3. Test Conditions

3.3.1. Establish and maintain test conditions in accordance with section 2.4 of this appendix.

3.4. Test Method and Measurements

3.4.1. Turn on all of the lamps at full light output.

3.4.2. Send a signal to the ballast instructing it to have zero light output using the appropriate ballast communication protocol or system for the ballast being tested.

3.4.3. Stabilize the ballast prior to measurement using one of the methods as specified in section 5 of IEC 62301.

3.4.4. Measure the standby mode energy consumption in watts using one of the methods as specified in section 5 of IEC 62301.

[FR Doc. 2020–14646 Filed 9–11–20; 8:45 am]

BILLING CODE 6450–01–P

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Part 701

RIN 3133–AF06

Chartering and Field of Membership

AGENCY: National Credit Union Administration (NCUA).

ACTION: Final rule.

SUMMARY: The NCUA Board (Board) is amending its chartering and field of membership (FOM) rules with respect to applicants and existing federal credit unions (FCUs) seeking a community charter approval, expansion, or conversion, in response to an August 2019 opinion and order issued by the D.C. Circuit Court of Appeals. First, the Board is re-adopting a provision to allow an applicant to designate a Combined Statistical Area (CSA), or an individual, contiguous portion thereof, as a well-defined local community (WDLC), provided that the chosen area has a population of 2.5 million or less. Second, with respect to communities based on a Core-Based Statistical Area (CBSA), or a portion thereof, the Board is providing additional explanation to support its decision to eliminate the requirement to serve the CBSA's core area as provided for in its comprehensive 2016 FOM rulemaking known as FOM1. Third, the Board is clarifying existing requirements and adding an explicit provision to its rules regarding potential discrimination in the FOM selection for CSAs and CBSAs.

DATES: This final rule is effective September 14, 2020.

FOR FURTHER INFORMATION CONTACT: For program issues: Martha Ninichuk, Director, or JeanMarie Komyathy, Deputy Director; Office of Credit Union Resources and Expansion, at 1775 Duke Street, Alexandria, VA 22314 or telephone (703) 518–1140. For legal issues: Ian Marenna, Associate General Counsel, or Marvin Shaw, Staff Attorney, Office of General Counsel, at the above address or telephone (703) 518–6540.

SUPPLEMENTARY INFORMATION:

I. Background

In a notice of proposed rulemaking and supplemental statement published on November 7, 2019,[1] the Board: (1) Proposed to re-adopt the presumptive WDLC option consisting of a CSA or an individual, contiguous portion of a CSA, provided that the chosen area, whether it is an entire CSA or a portion of one, is no more than 2.5 million;[2] (2) explained further, with additional reasoning and factual support, the basis for eliminating the core area service requirement for FCUs that choose a CBSA as a WDLC; and (3) proposed to amend the NCUA's regulations regarding community FOM applications, amendments, and expansions for CSAs and CBSAs to require the applicant to explain why it

[1] 84 FR 59989.

[2] References to CSAs or portions thereof in this final rule should be understood to carry this 2.5 million population limit. As noted above, an applicant may select an entire CSA as its WDLC if its population is 2.5 million or below. Alternatively, if the CSA's population is greater than 2.5 million, the applicant may still base its WDLC on the CSA, but must select an individual, contiguous portion of the CSA that has a population no greater than 2.5 million. Applicants also have the option of requesting areas outside these parameters. However, because these types of areas are not presumptive WDLCs, applicants must submit a narrative and supporting documentation establishing how the residents interact or share common interests. Please refer to NCUA Letter to Federal Credit Unions 18–FCU–02 (*https://www.ncua.gov/regulation-supervision/letters-credit-unions-other-guidance/requests-serve-well-defined-local-community-using-narrative-approach*) for additional background.

selected its FOM and to demonstrate that its selection will serve low- and moderate-income segments of a community. The proposed rule also included express authority for the NCUA to review and evaluate the foregoing explanation and submission regarding low- and moderate-income individuals, and to reject an application if the agency determines that the FCU's selection reflects discrimination. The Board proposed to apply this provision to CSAs and CBSAs. As detailed further below, the Board is adopting and finalizing all aspects of the proposed rule without change. The following sections provide background on this rulemaking.

A. Overview

Under the Federal Credit Union Act (Act), seven or more individuals may create an FCU by presenting a proposed charter (referred to in the Act as the organization certificate) to the Board.[3] These individuals, referred to as ''subscribers,'' must pledge to deposit funds for shares in the FCU and describe the FCU's proposed FOM.[4] An FOM consists of those persons and entities eligible for membership based on an FCU's type of charter. Before granting an FCU charter, the Board must complete an appropriate investigation and determine the character and fitness of the subscribers, the economic advisability of establishing the FCU, and the conformity of the proposed charter with the Act.[5] Under the Act, FCUs may choose from two general categories of FOM: Common-bond and community.[6]

The NCUA's Chartering and Field of Membership Manual, incorporated as Appendix B to Part 701 of the NCUA regulations (Chartering Manual),[7] implements the chartering and FOM requirements that the Act establishes for FCUs. The Chartering Manual provides that the NCUA will grant a charter if the FOM requirements are met, the subscribers are of good character and fit to represent the proposed FCU, and the establishment of the FCU is economically advisable.[8] In addition, ''[i]n unusual circumstances . . . [the] NCUA may examine other factors, such as other federal law or public policy, in deciding if a charter should be approved.''[9]

In adopting the Credit Union Membership Access Act of 1998 (CUMAA), which amended the Act, Congress reiterated its longstanding support for credit unions, noting their ''specific mission of meeting the credit and savings needs of consumers, especially persons of modest means.''[10] As amended by CUMAA, the Act provides a choice among three charter types: A single group sharing a single occupational or associational common bond;[11] a multiple common bond consisting of groups each of which have a distinct occupational or associational common bond among members of the group;[12] and a community consisting of ''persons or organizations within a well-defined local community, neighborhood, or rural district.''[13]

Congress expressly delegated to the Board substantial authority in the Act to define what constitutes a WDLC, neighborhood, or rural district for purposes of ''making any determination'' regarding a community FCU,[14] and to establish applicable criteria for any such determination.[15] To qualify as a WDLC, neighborhood, or rural district, the Board requires the proposed area to have ''specific geographic boundaries,'' such as those of ''a city, township, county (single or multiple portions of a county) or a political equivalent, school districts or a clearly identifiable neighborhood.''[16] The boundaries themselves may consist of political borders, streets, rivers, railroad tracks, or other static geographical features.[17] The Board continues to emphasize that common interests or interaction among residents within those boundaries are essential features of a local community.

Until 2010, the Chartering Manual required FCUs seeking to establish an area as a WDLC to submit for NCUA approval a narrative, supported by documentation, that demonstrated indicia of common interests or interaction among residents of a proposed community (the ''narrative model'') if the community extended beyond a single political jurisdiction (SPJ).[18] A WDLC was (and still is) required to consist of a contiguous area, as reflected in the current text of the Chartering Manual.[19] In 2010, the Board replaced the narrative model in favor of an objective model that provided FCUs a choice between two statistically based ''presumptive communities'' that each by definition qualifies as a WDLC (the ''presumptive community model'').[20] Further, the Board carefully considered the expertise and reasoning of the agencies that devised the statistical areas in deciding to designate these areas as WDLCs. In particular, the Board noted its agreement with the Office of Management and Budget (OMB) that commuting patterns within statistical areas demonstrate a high degree of social and economic integration with the central county.[21] Under the presumptive community model, approval is not automatic; rather, there is a multiple-step process. Once a presumptive WDLC is established, an FCU is still required to demonstrate its ability to serve its entire proposed community, as demonstrated by the required business and marketing plans. Then, the NCUA's staff, including the Office of Credit Union Resources and Expansion (CURE), the Office of General Counsel (OGC), and Regional Offices, review the application to ensure the applicant has established that it can serve its entire proposed community.

One kind of presumptive community is an ''[SPJ] . . . or any contiguous portion thereof,'' regardless of

[3] 12 U.S.C. 1753.

[4] 12 U.S.C. 1753(5).

[5] 12 U.S.C. 1754.

[6] 12 U.S.C. 1759(b).

[7] Appendix B to 12 CFR part 701 (Appendix B). The Chartering Manual is a single regulation that addresses all aspects of chartering FCUs. In that respect, it is similar to regulations of the Office of the Comptroller of the Currency (OCC) applicable to the chartering of national banks or federal savings associations. 12 CFR part 5.

[8] Appendix B, Ch. 1, section I.

[9] *Id.*

[10] Public Law 105–219, 2, 112 Stat. 913 (Aug. 7, 1998).

[11] 12 U.S.C. 1759(b)(1).

[12] *Id.* 1759(b)(2)(A).

[13] *Id.* 1759(b)(3).

[14] *Id.* 1759(g)(1)(A).

[15] *Id.* 1759(g)(1)(B). The Circuit Court cited this express delegation in its August 2019 decision, which is discussed in detail below. *Am. Bankers Ass'n* v. *Nat'l Credit Union Admin.,* 934 F.3d 649, 663 (D.C. Cir. 2019).

[16] Appendix B, Ch. 2, section V.A.2.

[17] Appendix B, Ch. 2, section V.A.5.

[18] 75 FR 36257 (June 25, 2010).

[19] Appendix B., Ch. 2., section V.A.2. The Chartering Manual also contained this requirement in 2003 under the narrative model. 68 FR 18334 (Apr. 15, 2003). ''The well-defined local community, neighborhood, or rural district may be met if: The area to be served is multiple contiguous political jurisdictions, *i.e.,* a city, county, or their political equivalent, or any *contiguous* portion thereof and if the population of the requested well-defined area does not exceed 500,000.'' (emphasis added). While the specific wording of this provision has been revised since 2003, the NCUA has always required that a WDLC consist of a contiguous area, dating back to 1999.

[20] As explained in the 2010 final rule that discontinued the use of the narrative model, the Board ''does not believe it is beneficial to continue the practice of permitting a community charter applicant to provide a narrative statement with documentation to support the credit union's assertion that an area containing multiple political jurisdictions meets the standards for community interaction and/or common interests to qualify as a WDLC. As [the proposed rule] noted, the narrative approach is cumbersome, difficult for credit unions to fully understand, and time consuming. . . . While not every area will qualify as a WDLC under the statistical approach, NCUA stated it believes the consistency of this objective approach will enhance its chartering policy, assure the strength and viability of community charters, and greatly ease the burden for any community charter applicant.'' 75 FR 36257, 36260 (June 25, 2010).

[21] 75 FR 36257, 36259 (June 25, 2010).

population.[22] The second is a single CBSA [23] (as defined above) as designated by the U.S. Census Bureau, or a well-defined portion thereof, which under the 2010 final rule was subject to a 2.5 million population limit.[24]

B. 2015 and 2016 Rulemakings

On November 19, 2015, the Board approved a proposed rule to amend various provisions of the Chartering Manual, including the WDLC and rural district options for community FOMs (2015 Proposed Rule).[25] As relevant here, in the 2015 Proposed Rule, the Board proposed to amend the community FOM options by: (1) Eliminating the requirement for an FCU serving a CBSA to serve its core area; (2) permitting FCUs to serve a portion of a CBSA up to a 2.5 million population limit, even if the CBSA's total population is greater than 2.5 million; [26] (3) permitting FCUs to serve CSAs,[27] which combine contiguous CBSAs, or a portion of a CSA, provided that the chosen area has a population no greater than 2.5 million; (4) permitting FCUs to apply to the NCUA to add adjacent areas to existing WDLCs consisting of SPJs, CBSAs, or CSAs, based on a showing of interaction by residents on both sides of the adjacent areas; and (5) increasing the population limit for rural district FOMs from the greater of 250,000 or 3 percent of the relevant state's population to 1 million, subject to a requirement that the rural district not expand beyond the states immediately contiguous to the state in which the FCU has its headquarters.

On October 27, 2016, the Board approved two rulemakings relating to the Chartering Manual. One was a final rule and the other a proposed rule. In the final rule,[28] the Board adopted the five provisions of the 2015 Proposed Rule that are set forth above (2016 Final Rule, which is also known as FOM1). In the proposed rule, the Board proposed additional changes to the community charter provisions (2016 Proposed Rule).[29] Specifically, the Board proposed permitting an applicant for a community charter to submit a narrative to establish the existence of a WDLC as an alternative to stand alongside the SPJ and presumptive statistical community options. According to the proposed rule, the proposed narrative model would serve the same purpose as in years prior to 2010, when the narrative model was used exclusively. Further, the Board proposed permitting an FCU to designate a portion of a statistical area as its community without regard to metropolitan division boundaries.

C. March 2018 Federal District Court Decision

The American Bankers Association (ABA) challenged several community FOM provisions adopted in the 2016 Final Rule under the Administrative Procedure Act (APA).[30] On March 29, 2018, the U.S. District Court for the District of Columbia (District Court) upheld, or left in place, three provisions and vacated two provisions of the 2016 Final Rule).[31] The court held that Congress had delegated sufficient statutory authority to the Board to issue such regulations under *Chevron* v. *Natural Resource Defense Council.*[32] Specifically, the court upheld the provision allowing an FCU to serve areas within a CBSA that do not include the CBSA's core, holding that the definition was a reasonable interpretation of ''local community'' and that the elimination of the core area service requirement was supported by the administrative record. The court also upheld the provision allowing an FCU to add an adjacent area to a presumptive community, similarly holding that this provision was reasonable under the Act, and that the Board chose reasonable factors to evaluate whether adjacent areas are part of the same local community. Also, the court upheld the elimination of the requirement that a CBSA as a whole have a population of no more than 2.5 million in order for even a portion of the CBSA to qualify as a WDLC, holding that the plaintiff had waived this challenge by failing to raise it in the rulemaking.

The District Court vacated the provision defining any individual portion of a CSA, up to a population limit of 2.5 million, as a WDLC, holding that it was contrary to the Act. Finally, the District Court vacated the provision to increase the population limit to 1 million people for rural districts, also finding it contrary to the Act.

Both parties appealed this decision. The NCUA appealed the court's rulings on CSAs and rural districts. The ABA appealed only the ruling on the core area service requirement. The CSA and rural district provisions remained vacated while the appeal was pending. Accordingly, the NCUA rescinded approvals granted under those provisions and ceased approving new applications. The NCUA filed a notice with the court on April 19, 2018, stating that it did not interpret the court's March 29, 2018, order as mandating de-listing of members who joined FCUs under the vacated provisions. The notice also stated that the ABA did not intend to seek an order de-listing such members.

D. 2018 Final Rule

On June 21, 2018, while the appeal was pending, the Board adopted certain limited aspects of the 2016 Proposed Rule in a final rule (2018 Final Rule).[33] Specifically, the 2018 Final Rule amended the Chartering Manual to: (1) Allow an FCU seeking to serve a community FOM to submit a narrative to support its chosen area, as an alternative to the presumptive community options; and (2) eliminate the requirement that a WDLC based on a CBSA must be confined to a single metropolitan division within a CBSA. For the narrative model for establishing a WDLC for a community FOM, the Board established a public hearing process for any such proposed

[22] Appendix B, Ch. 2, section V.A.2 of the Chartering Manual defines ''single political jurisdiction'' as ''a city, county, or their political equivalent, or any single portion thereof.''

[23] A CBSA is composed of the country's Metropolitan Statistical Areas and Micropolitan Statistical Areas. ''Metropolitan Statistical Areas'' are defined by OMB as having ''at least one urbanized area of 50,000 or more population, plus adjacent territory that has a high degree of social and economic integration with the core as measured by commuting ties.'' ''Micropolitan Statistical Areas'' are identical to Metropolitan Statistical Areas except that their urbanized areas are smaller, *i.e.,* the urbanized area contains at least 10,000 but fewer than 50,000 people. A ''Metropolitan Division'' is a subdivision of a large Metropolitan Statistical Area. Specifically, a Metropolitan Division is ''a county or group of counties within a Metropolitan Statistical Area that has a population core of at least 2.5 million.'' OMB Bulletin No. 15–01 (July 15, 2015).

[24] *Id.* ''A total population cap of 2.5 million is appropriate in a multiple political jurisdiction context to demonstrate cohesion in the community.'' 75 FR 36257, 36260 (June 25, 2010).

[25] 80 FR 76748 (Dec. 10, 2015).

[26] Similar to CSAs, as discussed in note 2, this provision allows an applicant to serve an entire CBSA if its population is no greater than 2.5 million. If the CBSA's population exceeds 2.5 million, an applicant may still base its WDLC on the CBSA but must select an individual, contiguous area that has a population no greater than 2.5 million.

[27] CSAs are composed of adjacent CBSAs that share what OMB calls ''substantial employment interchange.'' OMB characterizes CSAs as ''representing larger regions that reflect broader social and economic interactions, such as wholesaling, commodity distribution, and weekend recreational activities, and are likely to be of considerable interest to regional authorities and the private sector.'' OMB Bulletin No. 15–01.

[28] 81 FR 88412 (Dec. 7, 2016).

[29] 81 FR 78748 (Nov. 9, 2016).

[30] 5 U.S.C. 702.

[31] *Am. Bankers Ass'n* v. *Nat'l Credit Union Admin.,* 306 F. Supp. 3d 44 (D.D.C. 2018).

[32] 467 U.S. 837 (1984). Shortly after CUMAA's s enactment, the D.C. Circuit determined that the Board acted within its delegated authority to issue rules for multiple common bond and community charters under *Chevron* in *Am. Bankers Ass'n* v. *Nat'l Credit Union Admin,* 271 F.3d 262 (D.C. Cir. 2001).

[33] 83 FR 30289 (June 28, 2018).

community with a population greater than 2.5 million. Further, with regard to the change to CBSA limitations based on metropolitan division boundaries, no commenters objected to this technical change. In addition, in light of the March 2018 District Court Decision vacating the CSA option, the Board removed the CSA option from the Chartering Manual while it amended the portions of the Chartering Manual that contained this option. The 2018 Final Rule contained no statement on the validity of the CSAs or any other indication that the Board had decided to abandon or re-visit this definition. Because the 2016 Proposed Rule did not propose any changes to the rural district definition, the Board did not amend or remove the rural district provision in the 2018 Final Rule.

E. August 2019 Circuit Court Decision

On August 20, 2019, a three-judge panel of the D.C. Circuit Court of Appeals (Circuit Court) issued a decision on the appeal.[34] The Circuit Court, in a unanimous decision, found that the Board acted within its statutory authority and thus reversed the District Court's rulings on CSAs and rural districts and directed the District Court to enter summary judgment for the NCUA on both issues. The Circuit Court also reversed the ruling on the core area service requirement for CBSAs, remanding the issue to the agency for further explanation without vacating the provision.

With respect to CSAs and rural districts up to 1 million people, the Circuit Court held that both provisions are consistent with the Act and were reasonably explained. First, the court found the CSA provision consistent with the ''local community'' provision of the Act.[35] Further, the Circuit Court found that the CSA definition, which is based on commuting relationships, rationally advances the statutory purpose of ensuring an affinity or common bond among members.[36] The court also found that the definition rationally advances the Act's safety and soundness purposes.[37] On this point, the court found that allowing for larger communities could promote the economic viability of community FCUs.[38] The court also held that the 2018 Final Rule's removal of the CSA option from the Chartering Manual did not render that issue moot, citing evidence of the Board's intention to re-promulgate this provision if the court upheld it.[39]

Second, the court held that the expansion of the rural district definition to areas including 1 million people is consistent with the Act.[40] The court found that the term ''rural district'' does not connote specific population or geographic constraints.[41] The court also found that the Board reasonably explained the expansion, including the 2016 Final Rule's discussion of the agency's experience with several larger rural districts under the pre-2016 rule.[42]

On one limited issue, the Circuit Court asked for additional explanation in reversing the District Court's ruling on the core area service requirement and directed the District Court to enter summary judgment for the plaintiff on this provision and remand, without vacating, this provision to the agency for further explanation.[43] The Circuit Court held that this provision is consistent with the Act, but that the 2016 Final Rule did not adequately explain it in light of the concern that commenters raised about the potential for FCUs to engage in redlining or gerrymandering of CBSAs to avoid serving minority or low-income individuals.[44] Accordingly, the Circuit Court directed the District Court to remand this provision without vacating it, and noted that it expected the Board to act ''expeditiously.''[45] The Circuit Court did not prescribe a specific deadline or procedure for the Board to follow. Therefore, this provision and approvals that the agency has granted under it remain in effect.

Currently, the Chartering Manual does not contain CSAs or portions thereof as an option for a WDLC. As a result of the Circuit Court finding the Board acted within its authority, the Board proposed to re-adopt the provision allowing a CSA or an individual, contiguous portion of a CSA, to be a presumptive statistical-based WDLC, provided that the chosen area has a population of no more than 2.5 million. The 2016 Final Rule's expanded definition of rural districts remained in the Chartering Manual and was upheld by the court's decision. Accordingly, the Board did not address rural districts in the proposed rule.[46] Finally, the Board provided further explanation and support, and proposed to add a provision to the Chartering Manual with respect to potential discrimination to address the Circuit Court decision. The Board issued the proposed rule promptly after the decision in light of the Circuit Court's expectation that the agency act expeditiously to provide further explanation on the CBSA core area service requirement.

II. Summary of Proposed Rule and Further Explanation of Core Area Service Requirement

On November 7, 2019, the Board published a notice proposing to amend its FOM rules with respect to applicants for a community charter approval, expansion, or conversion, in response to the Circuit Court's August 2019 opinion and order. First, the Board proposed re-adopting a provision to allow an applicant to designate a CSA, or an individual, contiguous portion thereof, as a WDLC, provided that the chosen area has a population of 2.5 million or less. Second, with respect to communities based on a CBSA or a portion thereof, the Board provided additional explanation for its decision to eliminate the core service requirement in the 2016 Final Rule. Third, the Board clarified existing requirements and proposed to add an explicit provision to its rules regarding potential discrimination in the FOM selection for CSAs and CBSAs.

III. Summary of Comments on the Proposed Rule

The Board received approximately 128 comments, including from bank and credit union trade associations, state leagues and associations, credit unions, and banks. A number of banks submitted a form letter opposing the proposal, particularly with respect to the elimination of the core area service provision.

Credit union-affiliated commenters generally supported the proposal to reinstate the CSA provision and eliminate the CBSA core area service requirement for community charters. Several credit union-affiliated commenters opposed additional requirements for the marketing and business plan to establish service to core

[34] *Am. Bankers Ass'n* v. *Nat'l Credit Union Admin.,* 934 F.3d 649 (D.C. Cir. 2019).

[35] *Id.* at 664.

[36] *Id.* at 665.

[37] *Id.* at 665–66.

[38] *Id.* at 666.

[39] *Id.* at 661–62.

[40] *Id.* at 672.

[41] *Id.* at 672–73.

[42] *Id.* at 673.

[43] *Id.* at 674.

[44] *Id.* at 670.

[45] *Id.*

[46] On October 4, 2019, the ABA filed a petition for rehearing *en banc* with respect to the panel's ruling on the CSA and rural district provisions. The NCUA responded to this petition, upon order of the court, on November 21, 2019. On December 12, 2019, the D.C. Circuit issued a *per curiam* (summary) order denying the petition. The Circuit Court issued its mandate to terminate the appeal on December 31, 2019, and the District Court entered summary judgment in accordance with the mandate on January 7, 2020. On March 11, 2020, the ABA filed a petition for a writ for certiorari requesting the U.S. Supreme Court review the Circuit Court decision. On June 29, 2020, the Supreme Court denied the ABA's petition. 2020 WL 3492665.

areas or low- and moderate-income individuals, viewing such requirements as unnecessary and burdensome.

Banks and bank trade associations provided comments largely opposing the proposed rule and the Board's objectives. These comments focused on eliminating the core area service requirement. Approximately 113 banks submitted various form letters opposing the proposal to eliminate the core requirement. The form letters criticized the proposal, emphasizing their belief that ''urban core areas deserve access to financial services'' and that the proposal would result in redlining. These commenters advocated that the Board adopt provisions similar to those issued by bank regulatory agencies that implement the Community Reinvestment Act (CRA). Specifically, they requested community-chartered credit unions account for low-, moderate-, and middle-income census tracts being excluded from the FOM and whether financial services are adequately being provided to those areas. Further, these commenters requested that an FCU be required to explain how people in the excluded core can access credit facilities if the FCU does not include the core.

The ABA [47] stated that the CSA and CBSA core provisions were ''seriously flawed'' and should be withdrawn unless the Board made significant modifications. The ABA relied extensively on the District Court decision that was unanimously reversed by the Circuit Court. Details of the comments are provided below in the discussion of the final rule.

IV. Final Rule

A. General

The Board has determined that it is appropriate and consistent with the Act to adopt the FOM chartering provisions described above, as proposed. Accordingly, the Board is amending its FOM rules with respect to applicants for a community charter approval, expansion, or conversion, in response to the 2019 opinion and order issued by the Circuit Court. First, the Board is re-adopting the provision to allow an applicant to designate a CSA, or an individual, contiguous portion thereof, as a WDLC, provided that the chosen area has a population of 2.5 million or less. Second, with respect to communities based on a CBSA or a portion thereof, the Board is providing additional explanation and support for its decision to eliminate the requirement to serve the CBSA's core area, as provided for in the 2016 Final Rule. In light of comments and consistent with the Circuit Court decision, the Board is clarifying existing requirements and adding an explicit provision to its rules regarding potential discrimination in the FOM selection for CSAs and CBSAs. Each of these three topics is discussed below.

B. Statutory Background and General Principles

Before responding to specific comments, the Board believes it is appropriate to explain the overall statutory basis for its FOM regulations applicable to chartering FCUs. In Section 2 of CUMAA, Congress set forth its ''Findings'' as follows:

The Congress finds the following:

(1) The American credit union movement began as a cooperative effort to serve the productive and provident credit needs of individuals of modest means.

(2) Credit unions continue to fulfill this public purpose, and current members and membership groups should not face divestiture from the financial services institutions of their choice as a result of recent court action.

(3) To promote thrift and credit extension, a meaningful affinity and bond among members, manifested by a commonality of routine interaction, shared and related work experiences, interests, or activities, or the maintenance of an otherwise well understood sense of cohesion or identity is essential to fulfillment of credit unions' public mission.

(4) Credit unions, unlike many other participants in the financial services market, are exempt from Federal and most State taxes because they are member-owned, democratically operated, not-for-profit organizations generally managed by volunteer boards of directors and because they have the specific mission of meeting the credit and savings needs of consumers, especially persons of modest means.

(5) Improved credit union safety and soundness provisions will enhance the public benefit that citizens receive from these cooperative financial service institutions.

These congressional findings—to encourage and improve financial access to credit to people of modest means, to enhance consumer choice, community affinity and common bonds, and to promote the safety and soundness of credit unions—are bolstered by specific provisions of CUMAA. For instance, Title 1 of that law addresses ''credit union membership,'' including the express provision in section 109 for the Board to establish regulations to encourage the chartering of community and multiple common bond FCUs. This section includes provisions encouraging formation of FCUs to encourage providing financial services to underserved communities and people of modest means. Title II of CUMAA mandates that the Board protect the National Credit Union Share Insurance Fund (NCUSIF) by issuing stricter safety and soundness provisions, including enhanced accounting standards in section 201. Title III of CUMAA includes capitalization and net worth requirements to ''resolve the problems of the insured credit unions at the least possible long-term loss to the [NCUSIF].'' Title III also sets forth specific mandates, including issuing regulations for prompt corrective action; capitalization requirements (including the submission of net worth restoration plans; earnings retention requirements; and prior written approval requirements for credit unions that are not adequately capitalized); certification of NCUSIF equity ratios; increased share insurance premiums; and periodic evaluation of access to liquidity. Title IV of CUMAA includes assurances for independent decision making in connection with certain charter conversions. Congress patterned these safety and soundness provisions after provisions applicable to the Federal Deposit Insurance Corporation (FDIC) and other banking regulatory agencies to ensure the safety and soundness of banks and protect the FDIC's insurance fund.

As CUMAA indicates, Congress directed the Board to consider multiple responsibilities, including encouraging access for financial services to people of modest means, encouraging competition among providers of financial services, and protecting taxpayers by enhancing the safety and soundness of the credit union system and protecting the NCUSIF. In contrast, banks have a more limited focus, including the interests of shareholders. This is illustrated in the ABA's comment letter, which states that the organization ''represents banks of all sizes and charters and is the voice of the nation's $18 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard more than $414 trillion in deposits, and extend $10.4 trillion in loans.'' [48]

[47] The ABA's submission included approximately 350 pages (14 pages were new comments, and the remainder consisted of attachments that included the ABA's legal filings and the District Court and Circuit Court decisions discussed above).

[48] In contrast, Federal credit unions have $803 billion in assets, employ roughly 160,000 people, safeguard $670 billion in shares and deposits, and extended $561 billion in loans.

Although the ABA's comment seems to oppose the Board's authority to construe the statute and promulgate substantive FOM rules based on consideration of the purposes of the Act, the Circuit Court made clear that Congress entrusted the NCUA with an express delegation of authority to reasonably construe the statutory field of membership terms, and to promulgate appropriate rules.[49] The Board also wishes to clarify the record in light of inaccurate statements in parts of the ABA's comments and litigation motions (which were appended to the ABA's comment letter).[50] Examples of factual misstatements in the ABA's ''Petition for Rehearing En Banc for Appellee-Cross-Appellant,'' which the ABA attached to its comment on this rulemaking, include the following. The Board wishes to clarify and correct these points, which pertain to the rulemaking generally:

- The ABA states that CSAs ''automatically qualify as 'local communities' ''[51] and ''The agency retains no discretion to determine that any application of its 'local community' or 'rural district' rule is unreasonable.''[52] In fact, such a CSA would be a ''presumptive community'' for which an applicant requests approval and provides a business and marketing plan to support an application. Then, NCUA staff in CURE reviews the application and in consultation with OGC for legal issues and the Office of Examination and Insurance and the Regional Office for safety and soundness concerns, may grant, deny or seek additional information.
- The ABA incorrectly states that there were ''hundreds of examples—and not a single counter-example—showing the agency's definitions fall outside the reasonable range of ambiguity of those terms.''[53] In oral argument before the Circuit Court, on behalf of the Board, the Department of Justice provided several examples.[54]
- The ABA incorrectly states Congress added the term ''local'' in the 1998 Act and then the Supreme Court ''reversed one such effort which would have allowed credit unions to be comprised of multiple unrelated employer groups (*NCUA* v. *First Nat'l Bank & Trust,* 522 U.S. 479 (1998).[55] In fact, the Supreme Court ruling came first on February 25, 1998, and then several months later Congress enacted CUMAA on August 7, 1998, including adding the term ''local.'' Also, the term ''local'' applies to community charters, while the Supreme Court decision focused on associational common bonds.
- The ABA references ''as applied'' challenges in 2004 in Utah and 2008 in Pennsylvania.[56] In fact, these cases challenged the sufficiency of administrative determinations that the NCUA made under the narrative model to establishing a community charter; this is a regulatory framework which has not been in effect for over a decade and was superseded by the new presumptive community rules adopted by notice-and-comment rulemaking in 2010 and supplemented in 2016. Thus, these pre-2010 cases are not relevant to the current challenge to presumptive communities set forth in the 2016 Final Rule.

The ABA also errs in stating: ''The panel relied on a separate regulation that requires credit unions to submit a business plan showing how the credit union would serve the proposed 'local community.' ''[57] In fact, both the presumptive community provisions for CSAs and CBSAs and the business and marketing plan requirements are in the same regulation.[58] The ABA further argued that ''[t]he rule leaves the agency with no discretion to determine that a particular application of its rule is unreasonable.''[59] In fact, for the reasons noted above, approval for a presumptive community is not automatic; an applicant must establish through its business and marketing plan that it can serve the community, as the Circuit Court observed.[60] All charter applications involve an iterative process between an applicant and the agency, with agency staff requiring the applicant to make modifications in approximately 95 percent of these applications. The NCUA chartering process is in this regard comparable to those that the federal banking agencies administer.[61] For example the Federal Reserve Board's application materials state: ''Starting a bank involves a long organization process that could take a year or more, and permission from at least two regulatory authorities. Extensive information about the organizer(s), the business plan, senior management team, finances, capital adequacy, risk management infrastructure, and other relevant factors must be provided to the appropriate authorities.''[62]

C. Proposal To Re-Adopt the CSA Community Charter Option

The Board proposed allowing a CSA (or a single portion thereof) to be a presumptive WDLC, subject to a 2.5 million population limit. In the proposed rule, the Board proposed to re-adopt this option in light of the Circuit Court decision reversing the District Court and upholding this provision in the 2016 Final Rule. The Board observed that the factual record regarding CSAs is materially identical to what existed in 2016. The only change that the Board proposed from the CSA option adopted in the 2016 Final Rule is clarifying language in the text of the Chartering Manual on the requirement that an FCU select a single, contiguous portion of a CSA to meet the WDLC requirement. The Board sought comments on this proposed action generally and specifically requested comments beyond the many it considered when it first adopted the CSA provision in FOM1.

Commenters generally supported the proposal to readopt the CSA provision. The ABA was the only commenter opposing it; no other bank-affiliated commenter addressed this proposal. In contrast, credit union commenters stated that CSAs are ''sufficiently compact to promote interaction and common interests among its residents'' and thus qualify as a WDLC. Other commenters stated that re-proposing this provision is consistent with the evolution in servicing members, as technology, financial services, and communities change. One commenter stated that adopting the CSA option is consistent with OMB designations that establish that there are sufficient interactions and common interests. Some commenters provided examples of CSAs, noting that cities in a CSA are ''intrinsically linked through both recreation and work.''

[49] *Am. Bankers Ass'n,* 934 F.3d at 663.

[50] On a non-substantive point, the ABA in its petition for rehearing *en banc* incorrectly referred to the NCUA's organic statute as the National Credit Union Act. *Id.* at 3.

[51] *Id.* at 1.

[52] *Id.* at 8.

[53] *Id.* at 1–2.

[54] The DOJ brief noted that ''people can readily refer to the Combined Statistical Areas of Midland-Odessa in Texas, Appleton-Oshkosh-Neenah in Wisconsin, El Paso-Las Cruces on the Texas-New Mexico border, or Joplin-Miami on the Missouri-Oklahoma border as being 'local communities,' as these towns clearly share strong economic and social ties.''

[55] *Id.* at 3.

[56] *Id.* at 4.

[57] *Id.* at 16.

[58] The Chartering Manual is all contained within Appendix B.

[59] ABA Petition for Rehearing at 16.

[60] 934 F.3d at 668.

[61] *See* FDIC Deposit Insurance Handbook at *https://www.fdic.gov/regulations/applications/depositinsurance/handbook.pdf.* For the OCC's procedures, see 12 CFR part 5.

[62] See the Federal Reserve Board's procedures at *https://www.federalreserve.gov/faqs/banking_12779.htm.*

In opposing the proposal, the ABA stated that defining a CSA as a ''single local community'' is unreasonable and unlawful. The ABA largely relied on the District Court opinion, which was unanimously reversed by the Circuit Court. The ABA provided examples of CSAs that it believes might not be a WDLC and contended that CSAs have a ''daisy-chain nature'' in which opposite ends have little connection. It then stated that the Circuit Court indicated that some CSAs might not be a WDLC and thus could be challenged on an ''as applied'' basis. The ABA further stated that the term ''local community'' should not automatically include a CSA. Rather, it stated that any presumption that a CSA is a local community should be rebuttable. The ABA further stated that the Board should not adopt these provisions while litigation remains pending, including the possibility of an appeal to the Supreme Court.

After reviewing the comments in light of the unanimous Circuit Court decision to affirm the Board's adoption of a CSA as a presumptive community, the Board has determined that it is appropriate and consistent with the Act to amend the Chartering Manual to allow a CSA to be re-established as a presumptive WDLC. Much of the ABA's argument relied on the District Court decision that was unanimously rejected by the three-judge Circuit Court panel. In applying *Chevron,* the Circuit Court stated: ''We appreciate the District Court's conclusions, made after a thoughtful analysis of the Act. But we ultimately disagree with many of them. In this facial challenge, we review the rule not as armchair bankers or geographers, but rather as lay judges cognizant that Congress expressly delegated certain policy choices to the NCUA. After considering the Act's text, purpose, and legislative history, we hold the agency's policy choices 'entirely appropriate' for the most part. *Chevron,* 467 U.S. at 865.'' [63] With respect to CSAs, the Circuit Court, in rejecting the District Court's analysis, stated:

> In addition to being consistent with the Act's text, the Combined Statistical Area definition rationally advances the Act's underlying purposes. In the 1998 amendments, Congress made two relevant findings about purpose. First, legislators found ''essential'' to the credit-union system a ''meaningful affinity and bond among members, manifested by a commonality of routine interaction [;] shared and related work experiences, interests, or activities [;] or the maintenance of an otherwise well-understood sense of cohesion or identity.'' § 2, 112 Stat. at 914. Second, Congress highlighted the importance of ''credit union safety and soundness,'' because a credit union on firm financial footing ''will enhance the public benefit that citizens receive.'' [64]

The Circuit Court explicitly rejected the ABA's assertion that CSAs have a ''daisy chain'' nature, linking multiple metropolitan areas that have nothing to do with those at opposite ends of the chain. As the court stated:

> [T]he NCUA's definition does not readily create general, widely dispersed regions. *Cf. First Nat'l Bank III,* 522 U.S. at 502 (indicating that community credit unions may not be 'composed of members from an unlimited number of unrelated geographical units'. Combined Statistical Areas are geographical units well-accepted within the government. *See* [81 FR at 88414]. Because they essentially are regional hubs, the Combined Statistical Areas concentrate around central locations. . . . The NCUA rationally believed that such 'real-world interconnections would qualify as the type of mutual bonds suggested by the term 'local community.' . . . Thus, the agency reasonably determined that Combined Statistical Areas ''simply unif[y], as a single community,'' already connected neighboring regions. [*See* 81 FR at 88,415.] [65]

The ABA's misinterpretation of the *Chevron* doctrine was further repudiated by the entire Circuit Court, which rejected the ABA's petition for a rehearing *en banc.* The Board emphasizes that the ABA repeatedly misstates the regulatory framework for approving a presumptive community, both in its court filings and in its comment letter on the proposed rule. Under the regulatory provisions in the Chartering Manual, established by notice-and-comment rulemaking, there is no automatic approval of an application based on a CSA. Rather, an applicant would have to establish in its application that it can serve the entire community, as documented in its business and marketing plan. A further constraint on any such CSA or portion thereof is that its population cannot exceed 2.5 million people. As the Circuit Court noted:

> We might well agree with the District Court that the approval of such a geographical area would contravene the Act. But even so, the Association would need much more to mount its facial pre-enforcement challenge in this case. As the Supreme Court repeatedly has held, ''the fact that petitioner can point to a hypothetical case in which the rule might lead to an arbitrary result does not render the rule'' facially invalid. *Am. Hosp. Ass'n* v. *NLRB,* 499 U.S. 606, 619 (1991); *see also EPA* v. *EME Homer City Generation, L.P. (EME Homer),* 572 U.S. 489, 524 (2014) (''The possibility that the rule, in uncommon particular applications, might exceed [the agency]'s statutory authority does not warrant judicial condemnation of the rule in its entirety.''); *INS* v. *Nat'l Ctr. for Immigrants' Rights, Inc.,* 502 U.S. 183, 188 (1991) (''That the regulation may be invalid as applied in s[ome] cases . . . does not mean that the regulation is facially invalid because it is without statutory authority.''); *cf. Barnhart* v. *Thomas,* 540 U.S. 20, 29 (2003) (''Virtually *every* legal (or other) rule has imperfect applications in particular circumstances.'').
>
> Here, the Association's complaint and the District Court's accompanying worry strike us as too conjectural. The NCUA must assess the ''economic advisability of establishing'' the proposed credit union before approving it, [12 U.S.C. 1754], and as part of the assessment, the organizers must propose a ''realistic'' business plan showing how the institution and its branches would serve all members in the local community, *see* [12 CFR. part 701, app. B, ch. 1 section IV.D.] The Association has failed to demonstrate the plausibility of a local community that is defined like the hypothetical narrow, multi-state strip and accompanies a realistic business plan. And if the agency were to receive and approve such an application, a petitioner can make an as-applied challenge. *See, e.g., EME Homer,* 572 U.S. at 523–24; *Buongiorno,* 912 F.2d at 510.[66]

Thus, existing regulatory provisions guard against the extreme examples posited by the ABA, which claims incorrectly that the Board must approve them under the Chartering Manual. The Board agrees with the ABA and the Circuit Court that any application for a presumptive community, including one based on a CSA, can be challenged on an as applied, case-by-case basis. Given this regulatory framework, which is subject to judicial review, the Board agrees with the Circuit Court's reasoning in concluding that re-establishing the CSA as a presumptive community is entirely consistent with the express authority delegated to the Board by Congress. This provision also advances the Act's dual purposes of promoting common bonds while addressing safety and soundness considerations by ensuring that FCUs remain economically viable.

[63] *Am. Bankers Ass'n,* 934 F.3d at 656. *See also* with respect to CSAs: ''The NCUA possesses vast discretion to define terms because Congress expressly has given it such power. But the authority is not boundless. The agency must craft a reasonable definition consistent with the Act's text and purposes; that is central to the review we apply at *Chevron's* second step. Here, the NCUA's definition meets the standard.'' *Id.* at 664.

[64] *Id.* at 665–66.

[65] *Id.* at 666–67.

[66] *Id.* at 668.

B. Proposal: Elimination of the Core Requirement for CBSA Community Charters

In the proposed rule, the Board addressed the Circuit Court's concern regarding the potential for discriminatory redlining or gerrymandering of FOMs based on a portion of a CBSA that excludes the core area. In accordance with the Circuit Court's order, the Board provided further explanation for the provision of the 2016 Final Rule that eliminated the requirement for an FCU to serve the core area when it chooses to base its FOM on a portion of a CBSA. As background and context for these considerations, the Board explained differences between the chartering processes for FCUs and other types of financial institutions, with particular reference to the CRA provisions that Congress has applied solely to banks and federal savings associations. The Board explained that Congress intentionally excluded credit unions from the CRA and established a different regulatory framework for how credit unions provide financial services to low- and moderate-income people. In addition to differences between banks and credit unions, the Board further explained that Congress established different regulatory incentives for government-sponsored enterprises, such as Fannie Mae and Freddie Mac.

In addition to these legislative differences, the proposal set forth additional reasons, including quantitative data, to support its decision to eliminate the core area service requirement. To this end, the Board reviewed the record from the 2016 Final Rule and observed that removing the core area service requirement would better allow FCUs flexibility to serve low- or moderate-income segments of communities in areas outside the cores. The Board noted that this consideration is consistent with a view that credit union-affiliated commenters expressed in response to the 2015 Proposed Rule. After reviewing the judicial decisions in this matter and comment letters from the 2015 and 2016 rulemaking, the Board determined that enhancing flexibility is consistent with its decision to eliminate the core area service requirement.

As an independent basis to support this decision, the Board presented and considered supplemental data relating to CBSAs to further support eliminating the core area service requirement. The Board noted that the data showed that a substantial majority of core areas in CBSAs receive service from community FCUs. In addition, the Board identified several CBSAs in which low- or moderate-income individuals could receive greater access to financial services, if FCUs are permitted to serve an FOM consisting of the non-core areas of those CBSAs. Specifically, the Board observed that household income is sometimes higher in certain neighborhoods in a CBSA's core as compared to suburban areas in adjacent counties outside the core. Retaining the core area service requirement would often require an applicant to provide financial services to relatively wealthy individuals in high-income areas who have ample options for their financial needs. Thus, the Board reasoned that the requirement may result in a potential applicant for a community charter either not seeking a charter for the low- to moderate-income areas or expending resources on wealthier areas in the core that have less need for such new services and access to credit. Based on that analysis, the Board found that this requirement may decrease potential credit opportunities for low- and moderate-income segments of communities in some circumstances. By removing the core area service requirement provision, the Board anticipated that a potential FCU applicant could focus its limited resources to better serve such less affluent communities.

In addition to those examples and analysis, the Board considered data reflecting that community FCUs tend to serve most CBSA core areas across the country. The NCUA's data (which are publicly available) show that a substantial majority of CBSAs, including their core areas, are currently served by community-based FCUs. FCUs of various other charter types also serve core areas across the country. In addition, FCUs currently serve the entirety of several of the most populous SPJs in the country—Los Angeles County, California; Houston, Texas; Philadelphia, Pennsylvania; and San Antonio, Texas. If any of these pre-existing FCUs sought to modify their FOM to exclude an urban core, such a request would be subject to scrutiny by the NCUA to determine whether the FCU was engaged in discriminatory practices or whether it might leave the urban core underserved.[67] Moreover, any member of these pre-existing FCUs could alert the NCUA of any potentially discriminatory practices, for which the NCUA could take appropriate action.[68] Because of this expansive coverage of core areas by pre-existing community FCUs, the Board found further support that it is reasonable to eliminate the core area service requirement.

Furthermore, the Board noted that approximately 700 community-based FCUs are currently designated as low-income credit unions (LICUs) pursuant to the Act and the NCUA's regulations.[69] These FCUs have the potential to serve over 10 million members across the country. As directed by Congress, the NCUA accords this designation to credit unions that predominantly serve low-income members. By obtaining this designation, credit unions gain greater flexibility in accepting nonmember deposits,[70] are exempt from the aggregate loan limit on business loans that otherwise applies to all federally insured credit unions,[71] may offer secondary capital accounts to strengthen their capital base,[72] and gain access to grants and loans from the Community Development Revolving Loan Program for Credit Unions.[73] Accordingly, the Board observed that community-based FCUs have both strong incentives and a strong record of providing service to low-income segments of communities.

Separately, the Board cited the agency's experience in implementing this provision since 2016 as a further indication of the non-discriminatory bases that FCUs have for pursuing this option. For example, in applications granted by the agency between 2016 and 2019 under this provision, the agency identified no discrimination. The Board detailed the reasons that the three FCUs approved under this provision had for their FOM selection, which centered on limited capacity or the ability to serve areas outlying a heavily populated core area, such as New York City. In light of that actual record, in addition to the data and examples, the Board found that the risk of discrimination is minimal and that FCUs have invoked the subject provision to serve areas outside the core that would otherwise have been omitted if the core area service requirement had been in place.

Comments were mixed on whether it is appropriate to eliminate the core area service requirement. While every credit union-affiliated commenter that addressed this specific proposal supported it, bankers opposed the Board's decision to eliminate the core service requirement.

[67] The new provisions in the Chartering Manual, discussed in detail below, would address this issue. App. 1, Ch. V.A.8.

[68] *Id.*

[69] 12 U.S.C. 1757(6); 12 CFR 701.34.

[70] 12 U.S.C. 1757(6).

[71] 12 U.S.C. 1759a(b)(2)(A).

[72] 12 CFR 701.34(b)–(d). Credit unions must submit a secondary capital plan under § 701.34(b)(1) before issuing secondary capital accounts.

[73] 12 CFR 705.2.

Credit union-affiliated commenters stated that eliminating the core service requirement will not encourage discriminatory lending practices, noting that FCUs have a history of providing financial services to the underserved, and unlike banks do not have a history of redlining. Additional reasons commenters provided for supporting the proposal include that it:

• Allows an FCU to request an FOM that more reasonably fits its ability to serve, thereby facilitating services to potential customers and that requiring service to the entire core may unreasonably stretch an applicant's resources;

• Provides FCUs added flexibility to serve low- and moderate-income communities in areas outside the core;

• Allows FCUs to focus on how best to allocate limited resources to allow service to low-income members and areas;

• Accommodates changing demographics in which core areas are wealthier, while suburbs are more diverse but poorer;

• Recognizes that FCUs have valid business reasons for choosing to serve or not to serve a CBSA's core; and

• Provides the NCUA added authority to reject applications that may be based on discriminatory intent.

These commenters further stated that the ABA's lawsuit would limit access of some low-income people to financial services. Specifically, they argued that implementing outdated and burdensome CRA requirements would reduce flexibility to serve poorer communities because FCUs may be required to serve wealthier cores, while reducing service to poorer areas. Consistent with the proposed rule's discussion, a commenter cited a *New York Times* article identifying demographic changes in downtown populations in Raleigh, Brooklyn, Atlanta, Indianapolis, Philadelphia, Nashville, Houston, Denver, and Chicago.[74]

Commenters noted that even without additional requirements, FCUs—like banks—are subject to numerous anti-discrimination laws, and the NCUA[75] already has authority to oversee compliance. In addition to the Equal Credit Opportunity Act of 1974 (ECOA)[76] and the Fair Housing Act of 1968,[77] the Home Mortgage Disclosure Act (HMDA)[78] mandates that FCUs provide extensive data on lending practices, thereby providing an additional mechanism to identify discriminatory lending trends. Further, compliance with fair lending laws is a core responsibility of an FCU's board of directors. Also, similar to bank regulatory examiners, NCUA examiners, who are trained to identify fair lending violations, are empowered to take appropriate action against FCUs relating to lending activity.

In contrast, bank-affiliated commenters opposed eliminating the core requirement, stating:

• The NCUA did not address the Circuit Court's concern that a community credit union can engage in redlining or gerrymandering to create a community of higher-income members;

• The NCUA should consider the effect on excluded portions of communities, without regard to the business needs of the credit union, in light of FCUs' mission of serving those of modest means;

• The NCUA needs to consider access to full-service branches, even though not statutorily mandated;[79]

• The NCUA should substantiate the statement in the proposed rule regarding FCUs serving most CBSA core areas across the country;

• The proposed rule did not consider two Government Accountability Office (GAO) studies that conclude that credit unions serve a lower percentage of people of modest means than banks;

• The fact that some CBSAs have lower-income people outside the core does not justify a blanket rule permitting FCUs to exclude core areas;

• Credit unions should undergo examinations similar to the CRA reviews that bank regulators conduct;

• FCUs should demonstrate whether: (1) The revised geographic boundaries outside the core would result in more low- and moderate-income individual[80] populations being served, (2) financial services are provided to the excluded areas, and (3) the excluded area will have access to financial services;

• The NCUA's consumer compliance program is not sufficient to ensure compliance with consumer compliance laws;

• The NCUA's consumer compliance practices are not sufficient to safeguard against illegal discrimination, stating the NCUA conducted 25 fair lending exams in 2018 (less than 2013) even though credit unions have added 22 million members since 2013; and

• The NCUA's complaint process does not address nonmembers seeking FOM expansions.

Accordingly, some of the bank-affiliated commenters requested that the NCUA withdraw the proposal because, as the ABA opined, "credit unions have a special mission of serving persons of modest means" and that it is "the Board's responsibility to carry out this mission." These commenters further requested that the NCUA require that FCUs demonstrate a compelling interest or need to exclude urban cores. They also requested that the NCUA provide for public input to allow community groups to weigh in on excluding the core area.

In response to supplemental information in the proposed rule regarding income distribution within and outside the core in several CBSAs, several commenters provided specific examples of credit unions serving wealthier communities while not adding branches in less affluent communities. The ABA specifically referenced Cleveland and Detroit to illustrate charters that may be approved by the NCUA under this provision where they contended lower-income and minority residents might be excluded from the FOM. Similarly, a Michigan banker referenced a state-chartered credit union's activities in Michigan.[81] In addition, the ABA questioned the proposed rule's examples of CBSAs in which some portions—represented by ZIP codes—outside the core area have lower median income than the relevant core areas. The ABA questioned the use of ZIP codes because the NCUA's chartering rules do not recognize ZIP codes as WDLCs. The ABA also stated that the fact that there may be relatively affluent parts of the urban core of some CBSAs, in which median incomes exceed those in some outlying suburbs, does not justify a blanket rule that credit unions may

[74] Badger. E., Bui Q, & Gebeloff R (Apr. 27, 2019), "The Neighborhood is Mostly Black. The Home Buyers Are Mostly White," *The New York Times, available at: https://www.nytimes.com/interactive/2019/04/27/upshot/diversity-housing-maps-raleigh-gentrification.html.*

[75] The NCUA, along with the Consumer Financial Protection Bureau (CFPB), FDIC, Federal Reserve, and the OCC, is a member of the Federal Financial Institutions Examination Council (FFIEC), which coordinates the supervision of financial institutions,

[76] 15 U.S.C. 1691 *et. seq.*

[77] Public Law 90–284.

[78] Public Law 94–200.

[79] No bank-affiliated commenter directly addressed the proposed rule's discussion about how Congress established different regulatory structures to provide financial services for underserved people and communities for different financial institutions. Specifically, Congress mandated the CRA for banks and federal savings association. In contrast, Congress declined applying the CRA to credit unions; rather, understanding the differences among financial institutions, Congress tailored different incentives for credit unions and government sponsored enterprises to facilitate providing financial services to people in underserved communities.

[80] The commenters referred to these groups as "LMIs."

[81] The Board notes that because the credit union referenced by the banker is state-chartered, it is not subject to the NCUA's chartering rules.

exclude all, or any part of, the urban core from their service area. According to the ABA, such a rule would permit FCUs to choose to serve only high-income areas of the CBSA, while excluding low-income areas.

Based on its review of the comments along with incorporating the rationale set forth in the proposed rule, the Board has determined that eliminating the core area service requirement is appropriate and consistent with the Act. In doing so, the Board reiterates its statement in the proposed rule that it sees each of the supporting points that it set forth as sufficient on its own to support eliminating this requirement. Considered together, these points cumulatively provide a reasoned basis for this action. As noted above, in establishing its FOM requirements, the Board must consider both providing increased access to consumers of modest means and enhancing safety and soundness and protecting the NCUSIF (and thus taxpayers). Based on its experience in analyzing community charters in light of the statutory provisions, the Board has determined that eliminating the core service requirement advances these congressional mandates. As discussed in the proposal, affording applicants for community charters the flexibility to match their financial resources with an underserved community will increase the likelihood that more low- to moderate-income consumers will be served, and enhances safety and soundness, because the applicant will be better able to serve a community without over-extending its resources. The inflexible regulatory requirement suggested by the bankers would likely result in not only providing fewer underserved communities access to financial services, but may result in more credit union failures.

As discussed in the proposed rule, of the approximately 50 community charters reviewed by the agency since the 2016 Final Rule took effect, the Board has approved only three community charters in which the applicant requested a CBSA that excluded the core. As the following table reflects, these charters are primarily for FCUs with assets ranging from $158 million to $281 million.[82] Thus, they illustrate the critical need for enhanced flexibility by not mandating service to the core area. Such flexibility may be crucial to the FCU's decision to seek a community in an area, especially near a major—and expensive—population center such as New York City, Boston, Washington, DC, or Cleveland.

Credit union	City	State	Approx. assets	Approved community
Palisades FCU	Pearl River	NY	$181 mil	Rockland County, NY and Bergen County, NJ (population 1.2 million) is a portion of larger New York-Jersey City-White Plains, NY-NJ Metropolitan Division (core under former rule would have been either New York City or New York County (Manhattan).
NYMEO FCU	Frederick	MD	$281 mil	Montgomery, Washington, Carroll, and Howard Counties, Maryland and Jefferson and Berkley Counties, West Virginia.
LorMet Community FCU	Amherst	OH	$158 mil	Expanded community charter to serve Lorain County, Ohio and the cities of Westlake, Bay Village and Rocky River, located in Cuyahoga County, Ohio.

For instance, the LorMet Community FCU provides a direct, real world, response to the ABA's reference to the Cleveland CBSA. The Cleveland-Elyria Ohio MSA—centered in Cuyahoga County—has 980 census tracts [83] with a population of 2,057,009. It is comprised of the following counties with these populations: Cuyahoga County (Cleveland)—1,243,857, Geauga County—94,031, Lake County—230,514, Lorain County—309,461, and Medina County—150,439.

LorMet Community FCU has 18,778 current members, three branches, and assets of $158 million. It was originally a state chartered credit union that served employees of a single occupation. LorMet converted to a federal community charter in 2000 to better diversify due to downturns in domestic manufacturing activities. Specifically, Lorain County suffered automotive and other manufacturing plant closures. The FCU's original community charter served people who live, work, worship, or attend school in and businesses and other legal entities located in Lorain County, Ohio, which is directly adjacent to Cuyahoga's western border. LorMet sought to expand to three small towns in Cuyahoga: Westlake (population 32,293), Bay Village (population 15,328), and Rocky River (population 20,264). The combined populations of these three towns represent less than six percent of Cuyahoga's total population. The agency approved the community charter request, which would allow the credit union to expand its indirect loan program to attract new members. Management based the credit union's service area on the areas covered by two automobile dealers with longstanding involvement in the credit union's indirect loan program. The indirect loan program served as an important driver of the credit union's loan acquisition, growth, and income. Absent the Board's decision to eliminate the core area service requirement, it would be highly impracticable for LorMet to serve all of Cuyahoga County, which has a population approximately 400 percent larger than Lorain County and 20 times more than the proposed expansion, within existing resources.

Similarly, the Detroit-Warren-Dearborn CBSA—centered in Wayne County—has 1,594 census tracts with a population of 4,326,442. This CBSA also includes five other counties: Lapeer—population 88,028, Livingston—population 191,224, Macomb—population 874,759, Oakland—population 1,259,201, and St. Clair—population 159,337. With respect to the named counties, each of the core areas has census tracts with both lower-income residents and significant wealthy areas of gentrification. For instance, one of Detroit's most affluent neighborhoods, Gross Pointe, is in Wayne County. Ten miles away and on the border with Wayne County, both Oakland and Macomb counties have some of the poorest segments of the CBSA. Thus, relative wealth at times does not correlate with the county in which a resident lives, as distressed core areas often have affluent residents, and suburban counties adjacent to the core area have extremely poorer ones. Thus, similar to the proposal's examples of Washington, DC and Atlanta, the

[82] The Small Business Administration considers any financial institution with assets under $600 million a small business. *See* 13 CFR 121.201, ''Small Business Size Standards by NAICS.'' This designation includes credit unions as well as banks.

[83] Each census tract has approximately 3,200 residents, thus offering an opportunity for a wide disparity in incomes.

same situation holds true for Cleveland and Detroit.

Counties adjacent to Cleveland and Detroit have faced significant economic challenges due to the loss of manufacturing jobs. For instance, in Lorain County, both Ford and US Steel closed manufacturing plans; and in Macomb County, General Motors closed plants. Eliminating the core area service requirement makes it more likely that an FCU would seek a community charter in these economically distressed adjacent counties than if they were required to seek a charter for the entire CBSA. It would be economically far more difficult, and potentially impossible, for a smaller FCU to provide financial services to both the core county and adjacent areas.

While nothing in the Chartering Manual prohibits an applicant from pursuing a charter for an entire CBSA up to 2.5 million people, a mandate requiring such service may dangerously and needlessly increase risk by overextending the resources of an FCU, especially a smaller one.[84] As discussed above, mandating that a community charter applicant serve the named core communities such as Cuyahoga in Cleveland and Wayne in Detroit may result in two harmful outcomes. First, an overextended smaller FCU is more likely to fail. Second, a potential applicant faced with having to serve both the named core as well as an adjacent area might make the business decision not to pursue an application at all, thereby reducing access to financial services for some low- and moderate-income consumers. Therefore, providing FCUs with limited resources more options will provide more low- and moderate-income people greater access to financial services.

The ABA also questioned why the NCUA had not addressed two GAO studies regarding the credit union industry. The first study (GAO–07–29) from 2006 indicated that 31 percent of credit union customers are of ''modest means'' as compared to 41 percent of bank customers.[85] The second GAO study (GAO–04–91) from 2003 concluded that credit unions provide a ''slightly lower'' percentage of their mortgage loans to low- and moderate-income households than banks.[86] The age of the studies as well as data limitations cast significant doubt on their usefulness to this rulemaking.[87] GAO–07–29 was issued in 2006 and relied on two-year old (2004) data from the Survey of Consumer Finances (SCF). GAO–04–91 was issued in 2003 and based its analysis on 2001 mortgage data from the HMDA database. Further, as the GAO itself acknowledged in both studies, the limitations inherent to the data require caution in their interpretation. In the case of GAO–07–29, the study noted that ''as an approximation of income levels, SCF data have certain limitations for measuring the income characteristics of credit union members.'' [88] GAO–04–91 provided that ''relying on HMDA data to evaluate credit union service to low- and moderate-income households has limitations'' due to the smaller size of credit unions and the fact they generally make more consumer loans than residential mortgage loans.[89] Also, the two studies inconsistently distinguished between FCUs and state-chartered credit unions [90] in presenting the statistics that the ABA cites. Given the questionable utility of these outdated studies which relied on data that preceded the Subprime Mortgage Crisis and the Great Recession, the Board believes that its actual experience with implementing the rule along with the more timely data presented in the November 7, 2019, proposed rule, as well as in the earlier FOM rules, better reflect the relevant policy and legal considerations.

The Board also notes that the ABA contended that the small number of approvals under this provision since 2016 suggests that the Board lacks sufficient experience to support what it terms a ''sweeping conclusion'' that FCUs have legitimate, nondiscriminatory purposes for using this provision. To the contrary, the Board finds that these limited approvals confirm the Board's conclusion. As noted in the proposed rule, eliminating the core area service requirement may benefit FCUs with more limited resources. The fact that FCUs have not used this provision extensively, but rather more selectively, tends to dispel the ABA's stated concern that FCUs will use the provision to avoid serving low- and moderate-income people. Instead, the Board's experience in analyzing community charter applications, regardless of the volume of applications and approvals, tends to show that FCUs have used the provision as the Board expected.

Further, as noted in the proposed rule, in light of changes in demographics and population trends, many core areas have residents with higher incomes compared to proximately close areas outside the core. In the proposed rule, the Board provided examples of this phenomenon of CBSAs, including Washington, DC and Atlanta. Commenters provided support for this phenomenon of many other gentrifying CBSAs, including the *New York Times* story discussed above. This phenomenon is further reflected by the demographics in Detroit and Cleveland.[91] No commenter provided convincing arguments or information to counter this factual consideration.

Regarding the ABA's comment concerning the Washington, DC and Atlanta examples in the proposed rule and questioning the use of ZIP codes to delineate portions of these CBSAs, the Board notes that the ABA does not dispute the income figures or provide evidence that in such CBSAs, an FCU could use the CBSA provision without the core area service requirement to compose an FOM that would likely contain more low-income individuals than if the FCU served the core area to the exclusion of outlying areas. Regarding the use of ZIP codes, the Board agrees that these designations do not constitute WDLCs under the Chartering Manual. Rather, the different ZIP codes correlate with areas within these CBSAs and were used to illustrate varying median income levels within well-recognized segments of these communities. Further, ZIP codes are more readily understood by the general public than other geographic designations such as census tracts. Accordingly, the Board continues to believe that such examples illustrate the potential benefits of eliminating the core area service requirement for CBSAs.

Similarly, with respect to the ABA's contention that a blanket rule permitting omission of the core area is not justified by the fact that more affluent people reside inside the core areas (and less affluent ones live outside the core) in some CBSAs, the Board believes that the real life examples more appropriately reflect current demographic and corresponding housing and income

[84] As of March 31, 2020, 74 percent of all FCUs have total assets under $100 million. Further, 60 percent of community-based FCUs have total assets under $100 million.

[85] Gov't Accountability Office, *Greater Transparency Needed on Who Credit Unions Serve and on Senior Executive Compensation Arrangements,* GAO–07–29 (Nov. 2006).

[86] Gov't Accountability Office, *Financial Condition Has Improved, but Opportunities Exist to Enhance Oversight and Share Insurance Management,* GAO–04–91 (Oct. 2003).

[87] By comparison, if Congress relied on data that was 16 to 19 years out of date when it enacted CUMAA, the data would reflect the 9 to 18 percent mortgage rate environment of the late 1970s and early 1980s. *http://www.fedprimerate.com/mortgage_rates.htm.*

[88] *Supra* note 85, at 5.

[89] *Supra* note 86, at 5.

[90] State chartered credit unions are not subject to NCUA's Chartering regulations. Further, some states provide more expansive chartering opportunities.

[91] For example, Shaker Heights in Cuyahoga is one of Cleveland's most affluent neighborhoods.

trends. The Board acknowledges, as it did in the proposed rule, that the phenomenon of outlying areas outside the cores having higher incomes is not universal. It is true in some instances, and the Board finds that eliminating the core area service requirement will make it more likely that FCUs with limited resources can select FOMs with more low- and moderate-income people in a safe and sound manner. The ABA's unsubstantiated concern that FCUs may use this provision to exclude low- and moderate-income people in other instances does not override this significant benefit to the rule. Also, this concern is independently addressed by the new provision that the Board is adopting in the Chartering Manual, discussed below, to provide the agency more explicit authority to address the ABA's concern, if FCUs do attempt to use the provision in order to exclude low- and moderate-income people from their FOMs.

In addition, the Board considered the recommendation by many banks that FCUs should be subject to the same CRA reviews that the banks undergo. The Board finds this recommendation misplaced because it addresses community service and lending activity after an FCU selects its FOM. As the Board noted in the proposed rule and discussed in detail in the 2016 Final Rule, under the Chartering Manual, the agency conducts periodic reviews of FCUs to determine whether they are serving their communities as stated in their initial FOM applications. These periodic reviews are conducted in addition to fair lending and safety and soundness examinations. The bank commenters did not explain why these existing procedures are insufficient in their view and also did not explain how the strength of reviews that the agency conducts after FOM selection is relevant to the validity of the provisions addressing how FCUs may designate their FOMs in the first instance. As the Circuit Court observed, FOM selection and post-selection community service are distinct,[92] and the agency will continue to conduct these periodic reviews for their intended purpose. Accordingly, the Board has established two sets of requirements. The Chartering Manual's requirement for an applicant to submit a business and marketing plan is prospective in nature and requires an applicant for a new or expanded charter to provide information about how it intends to serve the new community. The business and marketing plan requirement is supplemented by the periodic review requirement, which specifies that agency staff will evaluate how well a credit union has served its new community.

The ABA also indicated that eliminating the core area service requirement would result in disparate treatment for minorities, stating that ''NCUA must consider whether approval of a proposed service area that excludes the urban core of the community will have a discriminatory *effect.*'' [93] Throughout the ABA's comments, it refers many times to ''low income or minority individuals.'' [94] The Board finds that this rule addresses potential disparate impact on low-income or minority individuals in several significant ways.

First, as detailed in the preceding section, based on the Board's consideration of the evidence and public comments, the Board finds that eliminating the core area service requirement is likely to enhance service to areas outlying the cores, which may allow FCUs to respond to the trend of low-income and minority individuals moving to suburbs in greater numbers than in the past. Thus, the Board is not persuaded that maintaining this chartering option and the flexibility it provides will by its nature have a disparate impact on low-income or minority people.

Second, as detailed in this rulemaking, in the 2016 Final Rule, and in the Circuit Court's August 2019 opinion,[95] many pre-existing FCUs serve core areas where low-income and minority residents live. The Board found in the 2016 Final Rule that its periodic reviews of community service and enforcement of applicable anti-discrimination laws effectively address discriminatory practices that might occur separate from the initial chartering process, and the Circuit Court found that these measures could address such discrimination. This established process and the agency's experience in its administration indicate that the agency is well-equipped to address discrimination in the chartering process as it has in the post-chartering phase without the need to adopt a disparate impact or effects-based standard.

Third, as a complement to the post-chartering review and regulation, the Board is adopting the new provisions in the Chartering Manual detailed in the section below to provide explicit authority for the Board to address intentional discrimination in the chartering process. These provisions also directly address the ABA's concern.

For each of these individual reasons, the Board concludes that this final rule addresses the ABA's concern. As noted in the Circuit Court's opinion, this final rule would not bar the ABA from challenging such approved applications on an as-applied basis. But, the ABA's concerns are unfounded and do not provide persuasive reasons not to adopt this final rule, which is consistent with the Act.

The Board also notes that the ABA's statement about LICUs not serving all people of modest means in the country is misplaced. The ABA contends that the proposed rule's discussion of LICUs is not persuasive because LICUs have potential to serve only 3 percent of the United States population and that 11 percent of the population is below the poverty line. The Board did not state that LICUs have the potential or do serve all people of modest means in the United States. Instead, the Board enumerated the benefits of low-income designation as further, independent support for its finding that FCUs are unlikely to engage in redlining or gerrymandering because there is a strong incentive to compose FOMs that have larger percentages of low-income people in order to attain this designation, as set forth in detail above and in the proposed rule.

Similarly, the Board observes that the ABA does not factually dispute the statement in the proposed rule that FCUs serve the majority of CBSA core areas in the country. The ABA, which has access to public data on FOMs across the country, did not adduce or provide any contrary information or specifically question the conclusion. This information, like the information about LICUs, constitutes further, independent support for affirming this provision. As amply illustrated in the proposed rule and in this final rule, it is not the sole basis for support, and nor is it necessary to sustain the provision given the other strong reasons detailed in the proposed rule. Nevertheless, the Board continues to find this fact compelling because it confirms that

[92] 934 F.3d at 670.

[93] Emphasis in original.

[94] The Board acknowledges that there may be overlap between low-income and minority groups. Nevertheless, the ABA should be aware that in applying statutes and the ensuing regulatory regime, the threshold issue is always whether Congress applied the provisions to that entity. In its comment, the ABA conflates the CRA's purpose of providing financial services to underserved areas with ''disparate impact'' considerations that affect minority borrowers. By contrast, in the ABA's extensive comments to an advance notice of proposed rulemaking issued by the OCC and FDIC, the ABA made no mention of disparate impact, suggesting it views these concepts as distinct. ABA Comment Letter, Reforming the Community Reinvestment Act Regulatory Framework, Docket ID OCC–2018–0008, *available at https://www.aba.com/-/media/documents/comment-letter/cl-cra20181115.pdf?rev=a8d598e9460341e78a4d76aa004dd244.*

[95] *Am. Bankers Ass'n,* 934 F.3d at 970.

FCUs provide services to a broad range of areas across the country, including CBSA core areas. In addition, in response to the ABA's supposition that the Board noted this fact to suggest that other institutions are doing the work of serving those of modest means, the Board emphasizes that the agency does and will continue to evaluate each individual application on its own merits. The fact that FCUs already provide services to many low- and moderate-income individuals reinforces that FCUs have a strong history of doing so.

Based on its experience with community chartering, as bolstered by this legal analysis of the statutes that address providing financial services to people of modest means, the Board has determined that its decision to eliminate the core service requirement is appropriate and consistent with the legislation. Not only does the flexibility afforded by this regulatory decision incentivize the chartering of more community-based FCUs to serve people of modest means, but allowing an applicant to tailor its community to its residents and particular circumstances will increase economic viability. Thus, FCUs will likely have fewer safety and soundness concerns and will be less likely to fail. The Board further notes that nothing in the rule precludes an FCU from serving an entire CBSA up to the 2.5 million population limit, just that such an FCU is not mandated to do so. Statistics provided in the proposed rule indicated that FCUs already provide financial services to the vast majority of CBSA core areas. Thus, the bankers' proffered concerns that many low- and moderate-income people will not obtain such access is without merit.

Further, the bankers' dismissive response to the various fair lending laws, such as ECOA, HMDA, and the Fair Housing Act to which FCUs are subject is without merit, particularly because banks are subject to the same statutes and regulations. The NCUA—along with the CFPB, FDIC, Federal Reserve, and OCC—is a member of the Federal Financial Institutions Examination Council (known as the FFIEC) and thus extensively coordinates with those agencies on consumer compliance programs. Like bank consumer compliance examiners, NCUA examiners seek to ensure compliance with these consumer protection statutes and regulations. Further, the boards of directors of both banks and credit unions are on notice and fully aware that compliance with such consumer safeguards is essential and that non-compliance with fair lending statutes expose them to reputational risk, legal risk, and compliance risk, including enforcement actions and fines.[96]

These safeguards provide further support for the Board's determination that it is appropriate to eliminate the core area service mandate. The Board notes that the core area service requirement is a regulatory provision adopted in 2010 by a notice-and-comment rulemaking and is not required by the Act. After several years of experience with the provision, the Board determined that this provision was not necessary to further the Act's purposes. Further, the Board notes that the ABA's request that the Board demonstrate a ''compelling interest or need'' to exclude the core misunderstands the applicable law. A fundamental principle of administrative law under the APA is that an agency is required to provide a rational basis that the rule is not ''arbitrary, capricious, an abuse of discretion or otherwise not in accordance with the law.''[97] As described above and consistent with the Circuit Court's decision, the agency's decision to eliminate the core requirement is fully consistent with and advances the statutory mandate as described in the ''Findings'' section and various provisions in CUMAA. Eliminating the provision not only furthers financial access to people of modest means, but enhances the safety and soundness of credit unions and the share insurance fund.

The bankers' additional request to allow for public input from community groups to weigh in on excluding core areas is neither necessary nor appropriate. By approving new FCU charters, the Board is expanding choices for consumers, including those of modest means, and providing additional competition to other financial institutions. Such expanded choice and competition is in the interest of all consumers. Nothing in the approval of a new FCU requires an individual or community group to do anything other than potentially benefit from expanded alternatives.

D. Added Provision in Chartering Manual Addressing Service to Low- and Moderate-Income Individuals

The Board proposed amending the Chartering Manual to clarify and bolster the NCUA's authority to review applications to serve community-based FOMs consisting of CSAs or CBSAs to ensure that the FCU's requested community is not selected in order to exclude low- or moderate-income individuals. Under current provisions in the Chartering Manual, an applicant must detail how it will implement its business and marketing plan; the unique needs of various demographic groups in the proposed community; how the FCU will market to each group, particularly underserved groups; which community based organizations the FCU will target for outreach efforts; the FCU's marketing and budget projections dedicating resources to reach new members; and the FCU's timetable for implementation. Under the proposed rule, an FCU would be required to demonstrate that its choice of FOM, including choosing not to serve the core, is based on sound legal and business judgment and not an attempt to redline or discriminate on an illegal basis. This provision was proposed to supplement existing requirements for applicants to submit acceptable business plans, which applies to all community-based FOM applications.

Separately, and to complement this proposed requirement, the Board proposed to amend the Chartering Manual to clarify and bolster the NCUA's authority to reject applications to serve community-based FOMs consisting of CSAs or CBSAs, if the agency determines that the FCU's application is based on discriminatory intent or a desire to exclude low- or moderate-income individuals. The Board stated that this provision, if adopted, would serve as an additional means to address the issue that the Circuit Court raised regarding redlining and other forms of illegal discrimination. This provision was proposed to add to the existing provisions under which applicants must submit acceptable business plans, which applies to all community-based FOM applications.

Further, to make certain that the agency has explicit discretion to ensure that the FCU applicant will not seek to exclude service to low- and moderate-income segments of communities, the Board proposed to amend the Chartering Manual to provide that the NCUA may require additional information on how the FCU's business needs support its selection, conduct any further inquiry that it deems appropriate, and reject either an initial charter application or an expansion or amendment request if the NCUA determines that a community-based FCU has chosen its specific geographic area in order to exclude low- or moderate-income or underserved people.

The Board further discussed how it would expect CURE, in consultation

[96] ''Wells Fargo, Philadelphia reach settlement in redlining lawsuit,'' *The American Banker, available at https://www.americanbanker.com/news/wells-fargo-philadelphia-reach-settlement-in-redlining-lawsuit.*

[97] 5 U.S.C. 706.

with other agency offices, to implement this provision if it were adopted. Specifically, without proposing to require applicants to submit extensive information that might slow down the overall application process, the Board stated that CURE might consider other information in determining whether further review is needed, including, but not limited to, inclusion or exclusion of predominantly low- or moderate-income census tracts within a statistical area, the statements and supporting information from the applicant FCU regarding how it intends to serve low- and moderate-income individuals, and, if applicable, the FCU's record of consumer compliance or fair lending violations.

The Board found that this approach is appropriate because it expands on the existing principle and provision in Chapter 1 of the Chartering Manual that the NCUA may examine other factors in unusual cases when deciding whether to grant a charter, including other federal laws and public policy.[98] Further, the Board observed that it would also be consistent with the purposes animating the NCUA's organic Act, which recognizes that FCUs ''have the specified mission of meeting the credit and savings needs of consumers, especially persons of modest means.'' [99]

Banks and a few credit union-affiliated commenters generally supported or did not address such additional requirements. One commenter stated that the NCUA needs to require heightened documentation and explanations for FCUs seeking to exclude the core and how low-income residents will be served. Thus, the commenter believed that it is appropriate for the NCUA to request additional information on how an FCU's business needs would support its selection. This commenter viewed such a provision as not unreasonably burdensome, given that the NCUA may request such information only as warranted. Those favoring what they termed ''reasonable'' requirements stated that the current policy provides that the NCUA will review FCUs' plans to ensure service to such people. One commenter stated the proposed additional requirements were consistent with the Circuit Court decision, which indicated the requirement should be more explicit in terms of demonstrating service to underserved individuals.

In addition to their general support of additional requirements (subject to recommendations to strengthen the requirements), bankers also requested they have advance notice and the opportunity to participate in administrative proceedings, which they viewed as necessary to prevent the Board from ''acting as a rubber stamp.'' The ABA suggested strengthening the new proposed factor by requiring FCUs to show that their chosen service area will advance the mission of serving low- and moderate-income persons and reiterated its assertion that an FCU's business needs should not justify excluding such persons. The ABA also reiterated that the NCUA should look at the effect on excluded parts of communities, and not just at discriminatory intent. Other bank-affiliated comments made similar recommendations for increasing the NCUA's scrutiny of such applications, including by allowing FCU members to vote on any proposal for an FCU to leave its portion of the community.

In contrast, several of the credit-union affiliated commenters opposed the proposed regulatory provisions, which they characterized as requiring an applicant to demonstrate nondiscrimination in service area selections that show an FCU's ability to serve underserved individuals. These commenters were concerned that the proposed procedures were unreasonably vague and that it was not clear what type of additional information FCUs need to submit to demonstrate service to people of modest means. Specifically, some commenters requested that the NCUA should expressly include examples of evidence like income distribution or other statistical evidence in the Chartering Manual and not just in the preamble. They also expressed concern that these requirements would unnecessarily complicate and delay the application process. Several commenters requested that the NCUA define what this section in the business plan should include (including through the issuance of model form or guidance) and requested that the section not be so overly complicated or lengthy that it will entail additional cost or significant time.

Commenters made several additional observations about the new requirements. Several commenters stated that certain information should not be required in the marketing and business plan submission. The inclusion or exclusion of certain census tracts should not raise negative inferences, provided that an FCU has stated a rational explanation, using sound business judgment for the area selected. Similarly, one commenter questioned the use of an FCU's record of consumer compliance or fair lending violations. The commenter stated the NCUA should clarify the basis for this criterion. Commenters identified other concerns, including the difficulty in determining whether an applicant was not choosing a service area based on discriminatory factors. One commenter stated that it should be NCUA's responsibility to prove discriminatory intent rather than the applicant's responsibility to disprove it. Another commenter expressed concern about the potential to increase safety and soundness risk by focusing on service to low-income areas.

After reviewing the comments, the Board has decided to adopt the modifications to the Chartering Manual's provisions addressing an FCU's ability to provide financial services to people of modest means, as proposed. The Board notes that some commenters characterized the requirement as placing the burden on applicants to establish conclusively that the requested community charter would not discriminate against people of modest means. This is not the case; the applicant will be required to provide a narrative in the business and marketing plan establishing that the requested community will provide financial services to people of modest means. CURE, along with other divisions in the agency, will review the plan to ensure that the applicant's requested community will in fact provide such services to people of modest means. CURE staff has the option of approving the application, requesting additional information, or rejecting the application. The final rule further clarifies the Chartering Manual by stating in the new provision that illegal discrimination will form a basis for rejection, consistent with the discussion in the proposed rule preamble [100] and building on the existing principle in Chapter 1 of the Chartering Manual that permits the agency to consider other federal laws in deciding on an application.

The Board emphasizes that these changes essentially make explicit what had been required with respect to providing communities with financial services. Specifically, an applicant's business and marketing plan for a community charter has been required and will continue to be required to establish that it can provide financial services to people of modest means by providing demographic information such as income, race, gender, and financial resources. In addition, an applicant will continue to provide in the business and marketing plan its near-term and longer-term plans with respect to types of financial products

[98] Appendix B, Ch. 1, Section I.

[99] 12 U.S.C. 1751 note.

[100] 84 FR 59998 (Nov. 7, 2019).

and services that may appeal to people of modest means. Such products include various savings accounts and loan programs (including first-time car-buying loans, 125 percent automobile financing, PALs and similar programs). Additionally, specific information continues to be required about advertising and marketing activities and potential branching considerations. Thus, the Board agrees with the ABA's comment that ''FCUs [should] show that their chosen service area will advance the mission of serving low- and moderate-income persons.'' The Board has determined that this provision will advance that mission.

The Board finds no utility or justification for the suggestion that it provide advance notice and the opportunity to participate in administrative proceedings. The new, excessively burdensome procedures suggested by the bankers would impose additional administrative and economic burdens on both the applicants—many of which are small entities—and agency staff. These burdens are unnecessary and counterproductive because, as noted elsewhere in this final rule, FOM and chartering determinations may already be challenged on an as applied, case-by-case basis. Further, the resulting delays and possible introduction of superfluous information in the charter approval process would defeat the purposes of the presumptive community model. As the Board noted in the preamble to the proposed rule, the model was adopted to expedite charter approvals through the use of objectively verifiable statistical data.[101]

In addition, the Board finds that the proposal to add express authority for the NCUA to reject an application in appropriate circumstances is reasonable. As discussed in the proposed rule, this proposed provision builds on the existing principle in the Chartering Manual that the NCUA may consider other laws and public policy in reviewing a charter application. Far from creating a vague standard, the proposed provision establishes a more concrete implementation of this principle in the specific context of service to low- and moderate-income segments of communities. Accordingly, the Board adopts this provision as proposed. The Board declines to introduce further prescriptive details or requirements into the Chartering Manual, or to establish specific deadlines for agency action, in order to maintain flexibility for the agency and applicants. Specifically, the Board has determined that it is neither necessary nor appropriate to establish a model form; however, the Board emphasizes that the Chartering Manual provides significant guidance on the preparation of charter applications. Providing a model form would reduce flexibility without any significant corresponding benefit. As the agency and FCUs gain experience with the new provision, which is closely tied to the existing provisions, the agency can consider the need for any additional guidance.

At the same time, the Board has considered the comments by the ABA and other bank-affiliated commenters recommending that the Board consider the effects of discrimination against low- and moderate-income people, as well as intent or purpose. Conversely, some credit union-affiliated commenters opined that the Board should not consider discriminatory effects or impact and sought clarification of the standard. After carefully considering these comments, the Board clarifies that under the new provision in the Chartering Manual, it will focus on evidence of discriminatory intent or purpose. This standard is consistent with the text of the provision, as proposed, which states that the Board will consider whether the FOM was selected ''in order to exclude'' low- and moderate-income people. Similarly, this standard is responsive to the concern that the Circuit Court raised about FCUs potentially engaging in gerrymandering or redlining, both of which signify intentional exclusion. Contrary to the suggestions of some of the bank-affiliated commenters, there is no legal requirement applicable to FCUs that would mandate imposing an effects-based standard.

Further, as an independent basis to decline to adopt this suggestion, the Board concludes that an effects-based standard would be inappropriate. First, there is no clear or easily applicable test for what would constitute an acceptable or unacceptable disparate effect. Second, the commenters provide no evidence to suggest that an effects test, rather than an intent or purpose test, would necessarily result in different approvals or disapprovals of prospective FCU charters or expansions or amendments to existing FCU charters. The Board believes it is appropriate to adopt an intent or purpose test initially, so that both FCUs and the agency can develop familiarity with the process. After developing that experience, it might be appropriate in the future for the Board to revisit the standard and determine whether an effect test would be desirable, manageable, or result in materially different outcomes.

Likewise, the Board disagrees with the ABA and some of the other bank-affiliated commenters that asserted that an FCU's limited resources should not, by itself, justify excluding portions of a CBSA or CSA. As the Board details in the section above, in some instances, this flexibility may enable FCUs to serve more low- and moderate-income people safely and soundly. No other legal standard applies that would require additional explanation. In any event, the Board does agree with the ABA and other bank-affiliated commenters that the explanation should be consistent with FCUs' mission of meeting the needs of people of modest means, as well as the statutory purpose of ensuring the safety and soundness of FCUs.

Accordingly, the Board has determined that it is appropriate to avoid overly prescriptive provisions that would mandate certain types of quantitative or other information (in addition to the substantial, detailed information that applicants already provide under the Chartering Manual's requirements). Specifically, the Board has determined that there is no need to require an applicant to provide specific income distribution data or census tract information in addition to the extensive information that applicants provide under existing provisions in the Chartering Manual. Requiring such additional information would be unreasonably burdensome and costly without corresponding benefits.

D. Miscellaneous Comments

With respect to timing, some credit unions stated the NCUA should act quickly and not delay finalizing the provisions. In contrast, bank trade associations commented that the rule was not ''ripe'' because neither the full Circuit Court[102] nor the Supreme Court had adjudicated the rule. Thus, in their opinion, the proposal was premature until ''all current legal challenges have been exhausted.'' They stated that such a final agency action could harm or confuse consumers. The Board is issuing this final rule after the Supreme Court's June 29, 2020 denial of the ABA's petition for a writ of certiorari. Therefore, this concern is rendered moot.

Commenters also raised a few issues that are outside the scope of this rulemaking. For instance, a few commenters stated that the NCUA should align the federal chartering rules with state rules, because several states

[101] *See* 84 FR 59989, 59991 (Nov. 7, 2019).

[102] Subsequent to the comment period closing date, the full D.C. Circuit denied the ABA's petition to review the decision *en banc.*

have more liberal rules, resulting in conversions from federal to state charters. The Board is aware that under the dual chartering system, state laws may differ from federal ones. The Board sought to enhance the federal charter through FOM1 and the other recent rulemakings, within the constraints of the Act. Given that state chartering laws are often more permissive than the Act, the Board sought to allow more expansive chartering opportunities at the federal level. This serves to foster parity between state and federal laws and is in the interest of providing access to more financial services and furthering safety and soundness.

Another commenter requested that the NCUA should issue guidance on use of the narrative in applications and best practices. The Board notes that further discussion of the narrative approach is beyond the scope of this rulemaking proposal.

One commenter stated its support for a provision in the proposal to allow an FCU to designate a portion of a CBSA as a WDLC without regard to metropolitan division boundaries. The Board notes that this issue was resolved in the Board's June 2018 final rule (referred to as FOM2).[103]

V. Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires the NCUA to prepare an analysis to describe any significant economic impact a regulation may have on a substantial number of small entities.[104] For purposes of this analysis, the NCUA considers small credit unions to be those having under $100 million in assets.[105] Although this final rule is anticipated to economically benefit FCUs that choose to charter, expand, or convert to a community charter, the NCUA certifies that it would not have a significant economic impact on a substantial number of small credit unions.

Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3501 *et seq.*) requires that the Office of Management and Budget (OMB) approve all collections of information by a Federal agency from the public before they can be implemented. Respondents are not required to respond to any collection of information unless it displays a current, valid OMB control number.

In accordance with the PRA, the information collection requirements included in this final rule has been submitted to OMB for approval under control number 3133–0015.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, the NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. Primarily because this final rule applies to FCUs exclusively, it will not have a substantial direct effect on the states, on the connection between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. The NCUA has determined that this final rule does not constitute a policy that has federalism implications for purposes of the executive order.

Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this final rule would not affect family well-being within the meaning of Section 654 of the Treasury and General Government Appropriations Act, 1999.[106]

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121) (SBREFA) generally provides for congressional review of agency rules.[107] A reporting requirement is triggered in instances where the NCUA issues a final rule as defined in the APA.[108] An agency rule, in addition to being subject to congressional oversight, may also be subject to a delayed effective date if the rule is a ''major rule.''[109] As required by SBREFA, the NCUA submitted this final rule to the OMB for it to determine if the final rule is a ''major rule'' for purposes of SBREFA. OMB determined that this final rule is not a major rule. The NCUA also will file appropriate reports with Congress and the Government Accountability Office so this rule may be reviewed.

List of Subjects in 12 CFR Part 701

Credit, Credit unions, Reporting and recordkeeping requirements.

By the National Credit Union Administration Board on July 30, 2020.

Gerard Poliquin,

Secretary of the Board.

For the reasons stated above, the Board is amending 12 CFR part 701, appendix B as follows:

PART 701—ORGANIZATION AND OPERATION OF FEDERAL CREDIT UNIONS

■ 1. The authority for part 701 continues to read as follows:

Authority: 12 U.S.C. 1752(5), 1755, 1756, 1757, 1758, 1759, 1761a, 1761b, 1766, 1767, 1782, 1784, 1785, 1786, 1787, 1788, and 1789. Section 701.6 is also authorized by 15 U.S.C. 3717. Section 701.31 is also authorized by 15 U.S.C. 1601 *et seq.;* 42 U.S.C. 1981 and 3601–3610. Section 701.35 is also authorized by 42 U.S.C. 4311–4312.

■ 2. In appendix B to part 701, in chapter 2, section V.A.2 is revised, section V.A.8 is added, and section V.B is revised to read as follows:

Appendix B to Part 701—Chartering and Field of Membership Manual

* * * * *

Chapter 2—Field of Membership Requirements for Federal Credit Unions

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V—Community Charter Requirements

* * * * *

V.A.2—Definition of Well-Defined Local Community and Rural District

In addition to the documentation requirements in Chapter 1 to charter a credit union, a community credit union applicant must provide additional documentation addressing the proposed area to be served and community service policies, as well as the business plan requirements set forth in this Chapter. An applicant must meet all of these requirements to obtain NCUA approval.

An applicant has the burden of demonstrating to NCUA that the proposed community area meets the statutory requirements of being: (1) Well-defined, and (2) a local community or rural district. The applicant also has the burden of demonstrating that with respect to the proposed community, it has the capacity to provide financial services to low- and moderate-income areas of the community. The agency will reject any application that fails to establish the criteria set forth above.

For an applicant seeking a community charter for a Statistical Area with multiple political jurisdictions with a population of 2.5 million people or more, the Office of Credit Union Resources and Expansion (CURE) shall: (1) Publish a notice in the **Federal Register** seeking comment from interested parties about the proposed community and (2) conduct a public hearing about this application.

''Well-defined'' means the proposed area has specific geographic boundaries.

[103] 83 FR 30289 (June 28, 2018).

[104] 5 U.S.C. 603(a).

[105] 80 FR 57512 (Sept. 24, 2015).

[106] Public Law 105–277, 112 Stat. 2681 (1998).

[107] 5 U.S.C. 801–804.

[108] 5 U.S.C. 551.

[109] 5 U.S.C. 804(2).

Geographic boundaries may include a city, township, county (single, multiple, or portions of a county) or a political equivalent, school districts, or a clearly identifiable neighborhood.

The well-defined local community requirement is met if:

• Single Political Jurisdiction—the area to be served is a recognized Single Political Jurisdiction, *i.e.,* a city, county, or their political equivalent, or any single portion thereof.

• Statistical Area—A statistical area is all or an individual portion of a Combined Statistical Area (CSA) or a Core-Based Statistical Area (CBSA) designated by the U.S. Census Bureau, including a Metropolitan Statistical Area. To meet the well-defined local community requirement, the CSA or CBSA or a portion thereof, must be contiguous and have a population of 2.5 million or less people. An individual portion of a statistical area need not conform to internal boundaries within the area, such as metropolitan division boundaries within a Core-Based Statistical Area.

• Compelling Evidence of Common Interests or Interaction—In lieu of a statistical area as defined above, this option is available when a credit union seeks to initially charter a community credit union; to expand an existing community; or to convert to a community charter. Under this option, the credit union must demonstrate that the areas in question are contiguous and further demonstrate a sufficient level of common interests or interaction among area residents to qualify the area as a local community. For that purpose, an applicant must submit for NCUA approval a narrative, supported by appropriate documentation, establishing that the area's residents meet the requirements of a local community.

To assist a credit union in developing its narrative, Appendix 6 of this Manual identifies criteria a narrative should address, and which NCUA will consider in deciding a credit union's application to: Initially charter a community credit union; to expand an existing community, including by an adjacent area addition; or to convert to a community charter. In any case, the credit union must demonstrate, through its business and marketing plans, its ability and commitment to serve the entire community for which it seeks NCUA approval.

An area of any geographic size qualifies as a Rural District if:

• The proposed district has well-defined, contiguous geographic boundaries;

• The total population of the proposed district does not exceed 1,000,000;

• Either more than 50% of the proposed district's population resides in census blocks or other geographic units that are designated as rural by either the Consumer Financial Protection Bureau or the United States Census Bureau, OR the district has a population density of 100 persons or fewer per square mile; and

• The boundaries of the well-defined rural district do not exceed the outer boundaries of the states that are *immediately contiguous* to the state in which the credit union maintains its headquarters (*i.e.,* not to exceed the outer perimeter of the layer of states immediately surrounding the headquarters state).

The common bond affinity groups that apply to well-defined local communities also apply to Rural Districts.

The requirements in Chapter 2, Sections V.A.4 through V.G also apply to a credit union that serves a rural district.

* * * * *

V.A.8—Community Selection Requirements and Review

The NCUA will not approve an application for a community charter consisting of all or a portion of a CSA or a CBSA, including an initial application, amendment, or expansion, unless the applicant demonstrates in its business and marketing plan that (1) the credit union will serve a community that is contiguous and (2) the credit union will provide financial services to low- and moderate-income and underserved people, and that the credit union has not selected its service area in order to exclude low- and moderate-income and underserved people or to engage in illegal discrimination. Upon receipt of this material, the NCUA will evaluate the business and marketing plan to ensure that low- and moderate-income and underserved people will be served and that the credit union has not selected the service area in order to exclude such people or to engage in illegal discrimination. This requirement is in addition to the requirement to document in the business and marketing plan the realistic assumptions that support the credit union's viability and its plan to serve its entire FOM.

The NCUA may conduct such further inquiry or evaluation as it deems appropriate, as authorized by 12 U.S.C. 1754 and consistent with the principles of this Manual, other federal laws, and public policy. If the NCUA determines that the credit union's submission is inaccurate or unsupported, it may deny that application on those grounds, regardless of whether the application satisfies the other criteria for initial chartering, amendment, or expansion.

V.B Field of Membership Amendments

A community credit union may amend its field of membership by adding additional affinities or removing exclusionary clauses. This can be accomplished with a housekeeping amendment.

A community credit union also may expand its geographic boundaries. Persons who live, work, worship, or attend school within the proposed well-defined local community, neighborhood or rural district must have common interests and/or interact. The credit union must follow the requirements of Section V.A.4 and Section V.A.8 of this chapter.

A community credit union that is based on a Single Political Jurisdiction, a Statistical Area (*e.g.,* Core Based Statistical Area or Combined Statistical Area) or a rural district may expand its geographic boundaries to add a bordering area, provided the area is well defined and the credit union demonstrates that persons who live, work, worship, or attend school within the proposed expanded community (*i.e.,* on both sides of the boundary separating the existing community and the bordering area) have common interests and/or interact. Such a credit union applying to expand its geographic boundaries to add a bordering area must follow a streamlined version of the business plan requirements of Section V.A.4 of this chapter and the expanded community would be subject to the corresponding population limit—2.5 million in the case of a Single Political Jurisdiction, or a Statistical Area and 1 million in the case of a rural district. The streamlined business plan requirements for adding a bordering area are:

• Anticipated marginal financial impact on the credit union of adding the proposed bordering area, including the need for additional employees and fixed assets, and the associated costs;

• A description of the current and, if applicable, proposed office/branch structure specific to serving the proposed bordering area;

• A marketing plan addressing how the new community will be served for the 24-month period after the proposed expansion of a community charter, including detailing how the credit union will address the unique needs of any demographic groups in the proposed bordering community not presently served by the credit union and how the credit union will market to any new groups; and

• Details, terms and conditions of any new financial products, programs, and services to be introduced as part of this expansion.

* * * * *

[FR Doc. 2020–16988 Filed 9–11–20; 8:45 am]

BILLING CODE 7535–01–P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 71

[Docket No. FAA–2020–0491; Airspace Docket No. 20–ASO–16]

RIN 2120–AA66

Amendment of Class E Airspace; Guntersville, AL

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Final rule.

SUMMARY: This action amends Class E airspace extending upward from 700 feet above the surface at Guntersville Municipal Airport-Joe Starnes Field (formerly Guntersville Municipal Airport), Guntersville, AL, to accommodate new area navigation (RNAV) global positioning system (GPS) instrument approach procedures serving this airport. This action also updates the geographic coordinates of the airport. Controlled airspace is necessary for the safety and management of instrument flight rules (IFR) operations in the area.

DATES: Effective 0901 UTC, November 5, 2020. The Director of the Federal

Register approves this incorporation by reference action under Title 1 Code of Federal Regulations part 51, subject to the annual revision of FAA Order 7400.11 and publication of conforming amendments.

ADDRESSES: FAA Order 7400.11D, Airspace Designations and Reporting Points, and subsequent amendments can be viewed online at *http://www.faa.gov/air_traffic/publications/.* For further information, you can contact the Airspace Policy Group, Federal Aviation Administration, 800 Independence Avenue SW, Washington, DC 20591; Telephone: (202) 267–8783. The Order is also available for inspection at the National Archives and Records Administration (NARA). For information on the availability of FAA Order 7400.11D at NARA, email *fedreg.legal@nara.gov* or go to *https://www.archives.gov/federal-register/cfr/ibr-locations.html.*

FOR FURTHER INFORMATION CONTACT: John Fornito, Operations Support Group, Eastern Service Center, Federal Aviation Administration, 1701 Columbia Ave, College Park, GA 30337; Telephone (404) 305–6364.

SUPPLEMENTARY INFORMATION:

Authority for This Rulemaking

The FAA's authority to issue rule regarding aviation safety is found in Title 49 of the United States Code. Subtitle I, Section 106 describes the authority of the FAA Administrator. Subtitle VII, Aviation Programs, describes in more detail the scope of the agency's authority. This rulemaking is promulgated under the authority described in Subtitle VII, Part A, Subpart I, Section 40103. Under that section, the FAA is charged with prescribing regulations to assign the use of airspace necessary to ensure the safety of aircraft and the efficient use of airspace. This regulation is within the scope of that authority as it amends Class E airspace at Guntersville Municipal Airport-Joe Starnes Field, Guntersville, AL, to support IFR operations in the area.

History

The FAA published a notice of prosed rulemaking in the **Federal Register** (85 FR 34148, June 3, 2020) for Docket No. FAA–2020–0491 to amend Class E airspace extending upward from 700 feet above the surface at Guntersville Municipal Airport-Joe Starnes Field, Guntersville, AL, from a 6.3-mile radius to a 7-mile radius. In addition, the FAA proposed to update the airport's name and geographic coordinates to coincide with the FAA's aeronautical database.

Interested parties were invited to participate in this rulemaking effort by submitting written comments on the proposal to the FAA. No comments were received.

Class E airspace designations are published in Paragraph 6005, of FAA Order 7400.11D, dated August 8, 2019, and effective September 15, 2019, which is incorporated by reference in 14 CFR 71.1. The Class E airspace designations listed in this document will be published subsequently in the Order.

Availability and Summary of Documents for Incorporation by Reference

This document amends FAA Order 7400.11D, Airspace Designations and Reporting Points, dated August 8, 2019, and effective September 15, 2019. FAA Order 7400.11D is publicly available as listed in the **ADDRESSES** section of this document. FAA Order 7400.11D lists Class A, B, C, D, and E airspace areas, air traffic routes, and reporting points.

The Rule

This amendment to Title 14 Code of Federal Regulations (14 CFR) part 71 amends Class E airspace extending upward from 700 feet above the surface at Guntersville Municipal Airport-Joe Starnes Field, Guntersville, AL, from a 6.3-mile radius to a 7-mile radius. In addition, the FAA updates the airport's name and geographic coordinates to coincide with the FAA's aeronautical database. These changes are necessary for continued safety and management of IFR operations in the area.

FAA Order 7400.11, Airspace Designations and Reporting Points, is published yearly and effective on September 15.

Regulatory Notices and Analyses

The FAA has determined that this regulation only involves an established body of technical regulations for which frequent and routine amendments are necessary to keep them operationally current. It therefore: (1) Is not a "significant regulatory action" under Executive Order 12866; (2) is not a "significant rule" under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979); and (3) does not warrant preparation of a regulatory evaluation as the anticipated impact is so minimal. Since this is a routine matter that only affects air traffic procedures an air navigation, it is certified that this rule, when promulgated, does not have a significant economic impact on a substantial number of small entities under the criteria of the Regulatory Flexibility Act.

Environmental Review

The FAA has determined that this action qualifies for categorical exclusion under the National Environmental Policy Act in accordance with FAA Order 1050.1F, "Environmental Impacts: Policies and Procedures," paragraph 5–6.5a. This airspace action is not expected to cause any potentially significant environmental impacts, and no extraordinary circumstances exist that warrant preparation of an environmental assessment.

Lists of Subjects in 14 CFR Part 71

Airspace, Incorporation by reference, Navigation (air)

Adoption of the Amendment

In consideration of the foregoing, the Federal Aviation Administration amends 14 CFR part 71 as follows:

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

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

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

§ 71.1 [Amended]

■ 2. The incorporation by reference in 14 CFR 71.1 of FAA Order 7400.11D, Airspace Designations and Reporting Points, dated August 8, 2019, effective September 15, 2019, is amended as follows:

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

* * * * *

ASO AL E5 Guntersville, AL [Amended]

Guntersville Municipal Airport-Joe Starnes Field, AL

(Lat. 34°24′22″ N, long. 86°15′39″ W)

That airspace extending upward from 700 feet above the surface within a 7-mile radius of Guntersville Municipal Airport-Joe Starnes Field.

Issued in College Park, Georgia, on September 4, 2020.

Andreese C. Davis,

Manager, Airspace & Procedures Team South, Eastern Service Center, Air Traffic Organization.

[FR Doc. 2020–20109 Filed 9–11–20; 8:45 am]

BILLING CODE 4910–13–P

DEPARTMENT OF HOMELAND SECURITY

Coast Guard

33 CFR Part 117

[Docket No. USCG–2018–0955]

RIN 1625–AA09

Drawbridge Operation Regulation; Belle River, LA

AGENCY: Coast Guard, DHS.

ACTION: Final rule.

SUMMARY: The Coast Guard is changing the operating schedule that governs the State Route 70 pontoon bridge across Belle River, mile 23.8, at Pierre Part, Assumption Parish, Louisiana. During June, July and August this bridge will open on signal on the hour from 6 a.m. to 10 p.m. This rule is being changed to decrease vehicle congestion during the summer.

DATES: This rule is effective October 14, 2020.

ADDRESSES: To view documents mentioned in this preamble as being available in the docket, go to *https://www.regulations.gov.* Type USCG–2018–0955 in the ''SEARCH'' box and click ''SEARCH.'' Click on Open Docket Folder on the line associated with this rule.

FOR FURTHER INFORMATION CONTACT: If you have questions on this rule, call or email Mr. Doug Blakemore, Eighth Coast Guard District Bridge Administrator; telephone (504) 671–2128, email *Douglas.A.Blakemore@uscg.mil.*

SUPPLEMENTARY INFORMATION:

I. Table of Abbreviations

CFR Code of Federal Regulations
DHS Department of Homeland Security
FR Federal Register
LADOTD Louisiana Department of Transportation and Development
OMB Office of Management and Budget
NPRM Notice of Proposed Rulemaking (Advance, Supplemental)
SR State Route
§ Section
U.S.C. United States Code

II. Background Information and Regulatory History

On April 16, 2019 the Coast Guard published a notice of temporary deviation from regulations entitled Drawbridge Operation Regulations, Belle River, LA in the **Federal Register** (84 FR 15581), to collect and analyze information on vehicle and vessel traffic congestion on SR 70 created when the drawbridge opens to vessel traffic during periods of high vehicle traffic. We received five comments. All were in favor of the regulation change.

On May 13, 2020 the Coast Guard published a notice of proposed rulemaking entitled Drawbridge Operation Regulations, Belle River, LA in the **Federal Register** (85 FR 28542), to seek public comments on whether the Coast Guard should consider modifying the current operating schedule to the SR70 drawbridge. We received 0 comments.

III. Legal Authority and Need for Rule

The Coast Guard is issuing this rule under authority 33 U.S.C. 499.

LADOTD requested to change the drawbridge operating schedule for the SR70 pontoon bridge across the Belle River, mile 23.8, at Pierre Part, Assumption, LA. This bridge currently opens on signal except that from 10 p.m. to 6 a.m., the draw opens on signal if at least four hours' notice is given. LADOTD requested to open the bridge on signal on the hour during June, July and August from 6 a.m. to 10 p.m. each day.

This waterway is heavily used by recreational vessels during the summer months. The bridge has a vertical clearance of zero feet in the closed to vessel traffic position and unlimited vertical clearance in the open to vessel traffic position.

During a 105 day period LADOTD measured the vehicle and vessel queues created when the bridge opened on the hour. LADOTDs analysis of this data demonstrated that opening the bridge on the hour (vice on signal) reduced the average vehicle queue from 105 vehicles to 25 vehicles. There were no vessel queues created by this change.

This change reduces vehicle congestion during summer months and provides for the reasonable needs of navigation.

IV. Discussion of Comments, Changes and the Final Rule

There were 5 comments during the temporary regulation change and no comments during the NPRM. The Coast Guard provided a comment period of 60 days during each of these changes. Based on the LADOTD data this rule decreases vehicle congestion and provides vessels with the reasonable ability to use the waterway. We identified no impacts on marine navigation with this rule.

V. Regulatory Analyses

The Coast Guard has developed this rule after considering numerous statutes and Executive Orders related to rulemaking. Below we summarize our analyses based on a number of these statutes and Executive Orders, and we discuss First Amendment rights of protesters.

A. Regulatory Planning and Review

Executive Orders 12866 and 13563 direct agencies to assess the costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits. Executive Order 13771 directs agencies to control regulatory costs through a budgeting process. This rule has not been designated a ''significant regulatory action,'' under Executive Order 12866. Accordingly, it has not been reviewed by the Office of Management and Budget (OMB) and pursuant to OMB guidance it is exempt from the requirements of Executive Order 13771.

This regulatory action determination is based on the lack of commercial vessel traffic on this waterway, and the recreational boats that routinely transit the bridge under the proposed schedule. Those vessels with a vertical clearance requirement of less than 9.7 feet above mean high water may transit the bridge at any time, and the bridge will open in case of emergency at any time. This regulatory action takes into account the reasonable needs of vessel and vehicular traffic.

B. Impact on Small Entities

The Regulatory Flexibility Act of 1980 (RFA), 5 U.S.C. 601–612, as amended, requires federal agencies to consider the potential impact of regulations on small entities during rulemaking. The term ''small entities'' comprises small businesses, not-for-profit organizations that are independently owned and operated and are not dominant in their fields, and governmental jurisdictions with populations of less than 50,000. The Coast Guard received 0 comments from the Small Business Administration on this rule. The Coast Guard certifies under 5 U.S.C. 605(b) that this rule will not have a significant economic impact on a substantial number of small entities.

While some owners or operators of vessels intending to transit the bridge may be small entities, for the reasons stated in section V.A. above, this rule will not have a significant economic impact on any vessel owner or operator.

Under section 213(a) of the Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121), we want to assist small entities in understanding this rule. If the rule would affect your small business, organization, or governmental jurisdiction and you have questions concerning its provisions or options for compliance, please contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section.

Small businesses may send comments on the actions of Federal employees who enforce, or otherwise determine compliance with, Federal regulations to the Small Business and Agriculture Regulatory Enforcement Ombudsman and the Regional Small Business Regulatory Fairness Boards. The Ombudsman evaluates these actions annually and rates each agency's responsiveness to small business. If you wish to comment on actions by employees of the Coast Guard, call 1–888–REG–FAIR (1–888–734–3247). The Coast Guard will not retaliate against small entities that question or complain about this rule or any policy or action of the Coast Guard.

C. Collection of Information

This rule calls for no new collection of information under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520).

D. Federalism and Indian Tribal Government

A rule has implications for federalism under Executive Order 13132, Federalism, if it has 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. We have analyzed this rule under that Order and have determined that it is consistent with the fundamental federalism principles and preemption requirements described in Executive Order 13132.

Also, this rule does not have tribal implications under Executive Order 13175, Consultation and Coordination with Indian Tribal Governments, because it does not have a substantial direct effect 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.

E. Unfunded Mandates Reform Act

The Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) requires Federal agencies to assess the effects of their discretionary regulatory actions. In particular, the Act addresses actions that may result in the expenditure by a State, local, or tribal government, in the aggregate, or by the private sector of $100,000,000 (adjusted for inflation) or more in any one year. Though this rule will not result in such an expenditure, we do discuss the effects of this rule elsewhere in this preamble.

F. Environment

We have analyzed this rule under Department of Homeland Security Management Directive 023–01, Rev.1, associated implementing instructions, and Environmental Planning Policy COMDTINST 5090.1 (series) which guide the Coast Guard in complying with the National Environmental Policy Act of 1969 (NEPA) (42 U.S.C. 4321–4370f). The Coast Guard has determined that this action is one of a category of actions that do not individually or cumulatively have a significant effect on the human environment. This rule promulgates the operating regulations or procedures for drawbridges and s categorically excluded from further review, under paragraph L49, of Chapter 3, Table 3–1 of the U.S. Coast Guard Environmental Planning Implementation Procedures.

Neither a Record of Environmental Consideration nor a Memorandum for the Record are required for this rule.

G. Protest Activities

The Coast Guard respects the First Amendment rights of protesters. Protesters are asked to contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section to coordinate protest activities so that your message can be received without jeopardizing the safety or security of people, places or vessels.

List of Subjects in 33 CFR Part 117

Bridges.

For the reasons discussed in the preamble, the Coast Guard amends 33 CFR part 117 as follows:

PART 117—DRAWBRIDGE OPERATION REGULATIONS

■ 1. The authority citation for part 117 continues to read as follows:

Authority: 33 U.S.C. 499; 33 CFR 1.05–1; and Department of Homeland Security Delegation No. 0170.1.

■ 2. Revise § 117.424 to read as follows:

§ 117.424 Belle River.

The draw of the SR70 bridge, mile 23.8 near Belle River, shall open on signal; except that, from 10 p.m. to 6 a.m., the draw shall open on signal if at least four hours notice is given, and from June 1 through August 31 the draw shall open on signal on the hour from 6 a.m. to 10 p.m. The bridge shall open anytime at the direction of the District Commander.

Dated: August 18, 2020.

John P. Nadeau,

Rear Admiral, U.S. Coast Guard, Commander, Eighth Coast Guard District.

[FR Doc. 2020–19475 Filed 9–11–20; 8:45 am]

BILLING CODE 9110–04–P

DEPARTMENT OF HOMELAND SECURITY

Coast Guard

33 CFR Part 165

[Docket Number USCG–2020–0525]

RIN 1625–AA00

Safety Zone; Victoria Barge Canal, Victoria, TX

AGENCY: Coast Guard, DHS.

ACTION: Temporary final rule.

SUMMARY: The Coast Guard is establishing a temporary safety zone for parts of the navigable waters of the Victoria Barge Canal from approximate position 28°30′49″ N, 096°48′08″ W to approximate position 28°31′48″ N, 096°48′172″ W. The safety zone is needed to protect personnel, vessels, and the marine environment from potential hazards associated with SH–35 bridge fender repair operations. Entry of vessels or persons into this zone is prohibited unless specifically authorized by the Captain of the Port Sector Corpus Christi.

DATES: This rule is effective without actual notice from September 14, 2020 through 5 p.m. on September 19, 2020. For purposes of enforcement, actual notice will be used 7 a.m. on August 31, 2020 through September 14, 2020.

ADDRESSES: To view documents mentioned in this preamble as being available in the docket, go to *https://www.regulations.gov,* type USCG–2020–0525 in the ''SEARCH'' box and click ''SEARCH.'' Click on Open Docket Folder on the line associated with this rule.

FOR FURTHER INFORMATION CONTACT: If you have questions on this rule, call or email Lieutenant Commander Margaret Brown, Sector Corpus Christi Waterways Management Division, U.S. Coast Guard; telephone 361–939–5130, email *Margaret.A.Brown@uscg.mil.*

SUPPLEMENTARY INFORMATION:

I. Table of Abbreviations

CFR Code of Federal Regulations
DHS Department of Homeland Security
FR Federal Register
NPRM Notice of proposed rulemaking
§ Section
U.S.C. United States Code

II. Background Information and Regulatory History

The Coast Guard is issuing this temporary rule without prior notice and opportunity to comment pursuant to authority under section 4(a) of the Administrative Procedure Act (APA) (5 U.S.C. 553(b)). This provision authorizes an agency to issue a rule without prior notice and opportunity to comment when the agency for good cause finds that those procedures are ''impracticable, unnecessary, or contrary to the public interest.'' Under 5 U.S.C. 553(b)(B), the Coast Guard finds that good cause exists for not publishing a notice of proposed rulemaking (NPRM) with respect to this rule because it is impracticable. We must establish this safety zone immediately and lack sufficient time to provide a reasonable comment period and then consider those comments before issuing the rule.

Under 5 U.S.C. 553(d)(3), the Coast Guard finds that good cause exists for making this rule effective less than 30 days after publication in the **Federal Register**. Delaying the effective date of this rule would be contrary to the public interest because immediate action is needed to respond to the potential safety hazards associated with the damaged fenders on the SH–35 Bridge.

III. Legal Authority and Need for Rule

The Coast Guard is issuing this rule under authority in 46 U.S.C. 70034. The Captain of the Port Sector Corpus Christi (COTP) is establishing a temporary safety zone for parts of the navigable waters of the Victoria Barge Canal from approximate position 28°30′49″ N, 096°48′08″ W to approximate position 28°31′48″ N, 096°48′172″ W. The safety zone is needed to protect personnel, vessels, and the marine environment from potential hazards associated with SH–35 bridge fender repair operations.

IV. Discussion of the Rule

This rule establishes a temporary safety zone August 31, 2020 through September 19, 2020, from 7 a.m. through 12 p.m. and 1 p.m. through 5 p.m. each day, Monday through Saturday and will be enforced during SH–35 bridge fender repairs. No vessel or person is permitted to enter the temporary safety zone during the enforcement period without obtaining permission from the COTP or a designated representative.

Persons or vessels seeking to enter the safety zone must request permission from the COTP or a designated representative on VHF–FM channel 16 or by telephone at 361–939–0450. If permission is granted, all persons and vessels shall comply with the instructions of the COTP or designated representative.

V. Regulatory Analyses

We developed this rule after considering numerous statutes and Executive orders related to rulemaking. Below we summarize our analyses based on a number of these statutes and Executive orders, and we discuss First Amendment rights of protestors.

A. Regulatory Planning and Review

Executive Orders 12866 and 13563 direct agencies to assess the costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits. Executive Order 13771 directs agencies to control regulatory costs through a budgeting process. This rule has not been designated a ''significant regulatory action,'' under Executive Order 12866. Accordingly, this rule has not been reviewed by the Office of Management and Budget (OMB), and pursuant to OMB guidance it is exempt from the requirements of Executive Order 13771.

This regulatory action determination is based on the size, location, and duration of the safety zone. This safety zone covers an area of the navigable waters of the Victoria Barge Canal from approximate position 28°30′49″ N, 096°48′08″ W to approximate position 28°31′48″ N, 096°48′172″ W for the purposes of SH–35 bridge fender repairs August 31, 2020 through September 19, 2020, from 7 a.m. through 12 p.m. and 1 p.m. through 5 p.m. each day, Monday through Saturday. Moreover, the Coast Guard will issue Local Notices to Mariners, Safety Marine Information Broadcasts, and Broadcast Notice to Mariners via VHF–FM marine channel 16 about the zone.

B. Impact on Small Entities

The Regulatory Flexibility Act of 1980, 5 U.S.C. 601–612, as amended, requires Federal agencies to consider the potential impact of regulations on small entities during rulemaking. The term ''small entities'' comprises small businesses, not-for-profit organizations that are independently owned and operated and are not dominant in their fields, and governmental jurisdictions with populations of less than 50,000. The Coast Guard certifies under 5 U.S.C. 605(b) that this rule will not have a significant economic impact on a substantial number of small entities.

While some owners or operators of vessels intending to transit the safety zone may be small entities, for the reasons stated in section V.A above, this rule will not have a significant economic impact on any vessel owner or operator.

Under section 213(a) of the Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121), we want to assist small entities in understanding this rule. If the rule would affect your small business, organization, or governmental jurisdiction and you have questions concerning its provisions or options for compliance, please contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section.

Small businesses may send comments on the actions of Federal employees who enforce, or otherwise determine compliance with, Federal regulations to the Small Business and Agriculture Regulatory Enforcement Ombudsman and the Regional Small Business Regulatory Fairness Boards. The Ombudsman evaluates these actions annually and rates each agency's responsiveness to small business. If you wish to comment on actions by employees of the Coast Guard, call 1–888–REG–FAIR (1–888–734–3247). The Coast Guard will not retaliate against small entities that question or complain about this rule or any policy or action of the Coast Guard.

C. Collection of Information

This rule will not call for a new collection of information under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520).

D. Federalism and Indian Tribal Governments

A rule has implications for federalism under Executive Order 13132, Federalism, if it has 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. We have analyzed this rule under that Order and have determined that it is consistent with the fundamental federalism principles and preemption requirements described in Executive Order 13132.

Also, this rule does not have tribal implications under Executive Order 13175, Consultation and Coordination with Indian Tribal Governments, because it does not have a substantial direct effect 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. If you believe this rule has implications for federalism or Indian tribes, please contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section above.

E. Unfunded Mandates Reform Act

The Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) requires Federal agencies to assess the effects of their discretionary regulatory actions. In particular, the Act addresses actions that may result in the expenditure by a State, local, or tribal government, in the aggregate, or by the private sector of $100,000,000 (adjusted for inflation) or more in any one year. Though this rule will not result in such an expenditure, we do discuss the effects of this rule elsewhere in this preamble.

F. Environment

We have analyzed this rule under Department of Homeland Security Directive 023–01 and Environmental Planning COMDTINST 5090.1 (series), which guide the Coast Guard in complying with the National Environmental Policy Act of 1969 (42 U.S.C. 4321–4370f), and have determined that this action is one of a category of actions that do not individually or cumulatively have a significant effect on the human environment. This rule involves establishment of a temporary safety zone for navigable waters of Victoria Barge Canal from approximate position 28°30′49″ N, 096°48′08″ W to approximate position 28°31′48″ N, 096°48′172″ W. The safety zone is needed to protect personnel, vessels, and the marine environment from potential hazards associated with SH–35 bridge fender repair operations. It is categorically excluded from further review under paragraph L60(a) in Table 3–1 of U.S. Coast Guard Environmental Planning Implementing Procedures 5090.1. A Record of Environmental Consideration supporting this determination is available in the docket where indicated under **ADDRESSES**.

G. Protest Activities

The Coast Guard respects the First Amendment rights of protesters. Protesters are asked to contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section to coordinate protest activities so that your message can be received without jeopardizing the safety or security of people, places or vessels.

List of Subjects in 33 CFR Part 165

Harbors, Marine safety, Navigation (water), Reporting and recordkeeping requirements, Security measures, Waterways.

For the reasons discussed in the preamble, the Coast Guard amends 33 CFR part 165 as follows:

PART 165—REGULATED NAVIGATION AREAS AND LIMITED ACCESS AREAS

■ 1. The authority citation for part 165 continues to read as follows:

Authority: 46 U.S.C. 70034, 70051; 33 CFR 1.05–1, 6.04–1, 6.04–6, and 160.5; Department of Homeland Security Delegation No. 0170.1.

■ 2. Add § 165.T08–0525 to read as follows:

§ 165.T08–0525 Safety Zone; Victoria Barge Canal, Victoria, TX.

(a) *Location.* The following area is a safety zone: All navigable waters of the Victoria Barge Canal from approximate position 28°30′49″ N, 096°48′08″ W to approximate position 28°31′48″ N, 096°48′172″ W. The safety zone is needed to protect personnel, vessels, and the marine environment from potential hazards associated with SH–35 bridge fender repair operations.

(b) *Effective period.* The section is effective August 31, 2020 through September 19, 2020, from 7 a.m. through 12 p.m. and 1 p.m. through 5 p.m. each day, Monday through Saturday.

(c) *Regulations.* (1) According to the general regulations in § 165.23 of this part, entry into this temporary safety zone is prohibited unless authorized by the Captain of the Port Sector Corpus Christi (COTP) or a designated representative.

(2) Persons or vessels seeking to enter the safety zone must request permission from the COTP on VHF–FM channel 16 or by telephone at 361–939–0450.

(3) If permission is granted, all persons and vessels shall comply with the instructions of the COTP or designated representative.

(d) *Information broadcasts.* The COTP or a designated representative will inform the public of the enforcement times and date for this safety zone through Broadcast Notices to Mariners, Local Notices to Mariners, and/or Safety Marine Information Broadcasts as appropriate.

Dated: September 1, 2020.

J.B. Gunning,

Captain, U.S. Coast Guard, Acting Captain of the Port Sector Corpus Christi.

[FR Doc. 2020–19853 Filed 9–11–20; 8:45 am]

BILLING CODE 9110–04–P

DEPARTMENT OF HOMELAND SECURITY

Coast Guard

33 CFR Part 165

[Docket Number USCG–2020–0543]

RIN 1625–AA00

Safety Zone; Corpus Christi Ship Channel, Corpus Christi, TX

AGENCY: Coast Guard, DHS.

ACTION: Temporary final rule.

SUMMARY: The Coast Guard is establishing a temporary safety zone for the navigable waters of the Corpus Christi Ship Channel within the Inner Harbor from position 27°49′7.80″ N, 097°28′28.69″ W to position 27°49′0.12″ N, 097°27′54.09″ W. The safety zone is needed to protect personnel, vessels, and the marine environment from potential hazards created by the salvage of the Dredge WAYMON BOYD adjacent to the channel. Entry of vessels into this zone is permitted with restrictions: Vessels shall not over take or pass other vessels within the zone, and vessels must operate at a slowbell only.

DATES: This rule is effective without actual notice from September 14, 2020 through 12 noon on September 15, 2020. For the purposes of enforcement, actual notice will be used from August 23, 2020 through September 14, 2020.

ADDRESSES: To view documents mentioned in this preamble as being available in the docket, go to *https://www.regulations.gov,* type USCG–2020–0543 in the ''SEARCH'' box and click ''SEARCH.'' Click on Open Docket Folder on the line associated with this rule.

FOR FURTHER INFORMATION CONTACT: If you have questions on this rule, call or email Lieutenant Commander Margaret Brown, Sector Corpus Christi Waterways Management Division, U.S. Coast Guard; telephone 361–939–5130, email *Margaret.A.Brown@uscg.mil.*

SUPPLEMENTARY INFORMATION:

I. Table of Abbreviations

CFR Code of Federal Regulations
DHS Department of Homeland Security
FR Federal Register
NPRM Notice of proposed rulemaking
§ Section
U.S.C. United States Code

II. Background Information and Regulatory History

The Coast Guard is issuing this temporary rule without prior notice and opportunity to comment pursuant to authority under section 4(a) of the

Administrative Procedure Act (APA) (5 U.S.C. 553(b)). This provision authorizes an agency to issue a rule without prior notice and opportunity to comment when the agency for good cause finds that those procedures are ''impracticable, unnecessary, or contrary to the public interest.'' Under 5 U.S.C. 553(b)(B), the Coast Guard finds that good cause exists for not publishing a notice of proposed rulemaking (NPRM) with respect to this rule because it is impracticable. We must establish this safety zone immediately and lack sufficient time to provide a reasonable comment period and then consider those comments before issuing the rule.

Under 5 U.S.C. 553(d)(3), the Coast Guard finds that good cause exists for making this rule effective less than 30 days after publication in the **Federal Register**. Delaying the effective date of this rule would be contrary to the public interest because immediate action is needed to respond to the potential safety hazards associated with the salvage of Dredge WAYMON BOYD.

III. Legal Authority and Need for Rule

The Coast Guard is issuing this rule under authority in 46 U.S.C. 70034. The Captain of the Port Sector Corpus Christi (COTP) has determined that potential hazards associated with the salvage of Dredge WAYMON BOYD. The purpose of this rule is to ensure safety of vessels and persons on these navigable waters in the safety zone.

IV. Discussion of the Rule

This rule establishes a temporary safety zone from August 23, 2020 through 12 noon September 15, 2020, and will be enforced during dredge salvage operations. Entry of vessels into this zone is permitted with restrictions: Vessels shall not over take or pass other vessels within the zone, and vessels must operate at a slowbell only.

Persons or vessels transiting the safety zone should check-in with the Harbormaster's Office 30 minutes prior to transit on VHF Channel 12 or 361–882–1773 to allow diving operations to safely secure if needed.

V. Regulatory Analyses

We developed this rule after considering numerous statutes and Executive orders related to rulemaking. Below we summarize our analyses based on a number of these statutes and Executive orders, and we discuss First Amendment rights of protestors.

A. Regulatory Planning and Review

Executive Orders 12866 and 13563 direct agencies to assess the costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits. Executive Order 13771 directs agencies to control regulatory costs through a budgeting process. This rule has not been designated a ''significant regulatory action,'' under Executive Order 12866. Accordingly, this rule has not been reviewed by the Office of Management and Budget (OMB), and pursuant to OMB guidance it is exempt from the requirements of Executive Order 13771.

This regulatory action determination is based on the size, location, and duration of the safety zone. This safety zone covers the navigable waters of the Corpus Christi Ship Channel within the Inner Harbor from position 27°49′7.80″ N, 097°28′28.69″ W to position 27°49′0.12″ N, 097°27′54.09″ W for the purposes of protecting personnel and the environment from dangers created by the salvage of Dredge WAYMON BOYD. Moreover, the Coast Guard will issue Local Notices to Mariners, Safety Marine Information Broadcasts, and Broadcast Notice to Mariners via VHF–FM marine channel 16 about the zone.

B. Impact on Small Entities

The Regulatory Flexibility Act of 1980, 5 U.S.C. 601–612, as amended, requires Federal agencies to consider the potential impact of regulations on small entities during rulemaking. The term ''small entities'' comprises small businesses, not-for-profit organizations that are independently owned and operated and are not dominant in their fields, and governmental jurisdictions with populations of less than 50,000. The Coast Guard certifies under 5 U.S.C. 605(b) that this rule will not have a significant economic impact on a substantial number of small entities.

While some owners or operators of vessels intending to transit the safety zone may be small entities, for the reasons stated in section V.A above, this rule will not have a significant economic impact on any vessel owner or operator.

Under section 213(a) of the Small Business Regulatory Enforcement Fairness Act of 1996 (Pub. L. 104–121), we want to assist small entities in understanding this rule. If the rule would affect your small business, organization, or governmental jurisdiction and you have questions concerning its provisions or options for compliance, please contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section.

Small businesses may send comments on the actions of Federal employees who enforce, or otherwise determine compliance with, Federal regulations to the Small Business and Agriculture Regulatory Enforcement Ombudsman and the Regional Small Business Regulatory Fairness Boards. The Ombudsman evaluates these actions annually and rates each agency's responsiveness to small business. If you wish to comment on actions by employees of the Coast Guard, call 1–888–REG–FAIR (1–888–734–3247). The Coast Guard will not retaliate against small entities that question or complain about this rule or any policy or action of the Coast Guard.

C. Collection of Information

This rule will not call for a new collection of information under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520).

D. Federalism and Indian Tribal Governments

A rule has implications for federalism under Executive Order 13132, Federalism, if it has 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. We have analyzed this rule under that Order and have determined that it is consistent with the fundamental federalism principles and preemption requirements described in Executive Order 13132.

Also, this rule does not have tribal implications under Executive Order 13175, Consultation and Coordination with Indian Tribal Governments, because it does not have a substantial direct effect 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. If you believe this rule has implications for federalism or Indian tribes, please contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section above.

E. Unfunded Mandates Reform Act

The Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) requires Federal agencies to assess the effects of their discretionary regulatory actions. In particular, the Act addresses actions that may result in the expenditure by a State, local, or tribal government, in the aggregate, or by the private sector of $100,000,000 (adjusted for inflation) or more in any one year. Though this rule will not result in such an expenditure, we do discuss the effects of this rule elsewhere in this preamble.

F. Environment

We have analyzed this rule under Department of Homeland Security Directive 023–01 and Environmental Planning COMDTINST 5090.1 (series), which guide the Coast Guard in complying with the National Environmental Policy Act of 1969 (42 U.S.C. 4321–4370f), and have determined that this action is one of a category of actions that do not individually or cumulatively have a significant effect on the human environment. This rule involves establishment of a temporary safety zone for the navigable waters of the Corpus Christi Ship Channel within the Inner Harbor from position 27°49′7.80″ N, 097°28′28.69″ W to position 27°49′0.12″ N, 097°27′54.09″ W. The safety zone is needed to protect personnel, vessels, and the marine environment from potential hazards created by salvage Dredge WAYMON BOYD. It is categorically excluded from further review under paragraph L60(a) in Table 3–1 of U.S. Coast Guard Environmental Planning Implementing Procedures 5090.1. A Record of Environmental Consideration supporting this determination is available in the docket where indicated under **ADDRESSES**.

G. Protest Activities

The Coast Guard respects the First Amendment rights of protesters. Protesters are asked to contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section to coordinate protest activities so that your message can be received without jeopardizing the safety or security of people, places or vessels.

List of Subjects in 33 CFR Part 165

Harbors, Marine safety, Navigation (water), Reporting and recordkeeping requirements, Security measures, Waterways.

For the reasons discussed in the preamble, the Coast Guard amends 33 CFR part 165 as follows:

PART 165—REGULATED NAVIGATION AREAS AND LIMITED ACCESS AREAS

■ 1. The authority citation for part 165 continues to read as follows:

Authority: 46 U.S.C. 70034, 70051; 33 CFR 1.05–1, 6.04–1, 6.04–6, and 160.5; Department of Homeland Security Delegation No. 0170.1.

■ 2. Add § 165.T08–0543 to read as follows:

§ 165.T08–0543 Safety Zone; Corpus Christi Ship Channel, Corpus Christi, TX

(a) *Location.* The following area is a safety zone: The navigable waters of the Corpus Christi Ship Channel within the Inner Harbor from position 27°49′7.80″ N, 097°28′28.69″ W to position 27°49′0.12″ N, 097°27′54.09″ W.

(b) *Effective period.* The section is effective from August 23, 2020 through 12 noon on September 15, 2020.

(c) *Regulations.* (1) According to the general regulations in § 165.23 of this part, Entry of vessels into this zone is permitted with restrictions: Vessels shall not over take or pass other vessels within the zone, and vessels must operate at a slowbell only.

(d) *Information broadcasts.* The COTP or a designated representative will inform the public of the enforcement times and date for this safety zone through Broadcast Notices to Mariners, Local Notices to Mariners, and/or Safety Marine Information Broadcasts as appropriate.

Dated: September 1, 2020.

J.B. Gunning,

Captain, U.S. Coast Guard, Acting Captain of the Port Sector Corpus Christi.

[FR Doc. 2020–19854 Filed 9–11–20; 8:45 am]

BILLING CODE 9110–04–P

ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 52

EPA–R09–OAR–2019–0655; FRL–10012–28–Region 9 Air Plan Approval; California; San Joaquin Valley Unified Air Pollution Control District and Feather River Air Quality Management District

AGENCY: Environmental Protection Agency (EPA).

ACTION: Final rule.

SUMMARY: The Environmental Protection Agency (EPA) is taking final action to approve revisions to the San Joaquin Valley Unified Air Pollution Control District (SJVUAPCD or District) and the Feather River Air Quality Management District (FRAQMD) portions of the California State Implementation Plan (SIP) under the Clean Air Act (CAA or Act). For the SJVUAPCD, these revisions concern a rule intended to track information related to emissions of volatile organic compounds (VOCs) and particulate matter (PM) from commercial charbroilers, and an administrative rule for the registration of certain emission units historically exempted from the SJVUAPCD's permit requirements. We are approving into the California SIP amendments to a SJVUAPCD local rule, which require owners and operators of commercial underfired charbroilers to submit a one-time information report and which subject certain underfired charbroilers to registration and weekly recordkeeping requirements. We are also approving a SJVUAPCD rule addressing registration requirements for these and certain other emission units. For the FRAQMD, these revisions concern a negative declaration for the Control Techniques Guidelines (CTG) for the Oil and Natural Gas Industry.

DATES: This rule is effective October 14, 2020.

ADDRESSES: The EPA has established a docket for this action under Docket ID No. EPA–R09–OAR–2019–0655. All documents in the docket are listed on the *https://www.regulations.gov* website. Although listed in the index, some information is not publicly available, *e.g.,* Confidential Business Information (CBI) or other information the disclosure of which is restricted by statute. Certain other material, such as copyrighted material, is not placed on the internet and will be publicly available only in hard copy form. Publicly available docket materials are available through *https://www.regulations.gov,* or please contact the person identified in the **FOR FURTHER INFORMATION CONTACT** section for additional availability information.

FOR FURTHER INFORMATION CONTACT: Stanley Tong, EPA Region IX, 75 Hawthorne St., San Francisco, CA 94105. By phone: (415) 947–4122 or by email at *tong.stanley@epa.gov.* Or Nicole Law, EPA Region IX, 75 Hawthorne St., San Francisco, CA 94105. By phone: (415) 947–4126 or by email at *law.nicole@epa.gov.*

SUPPLEMENTARY INFORMATION: Throughout this document, ''we,'' ''us'' and ''our'' refer to the EPA.

Table of Contents

I. Proposed Action
II. Public Comments and EPA Responses
III. EPA Action
IV. Incorporation by Reference
V. Statutory and Executive Order Reviews

I. Proposed Action

On May 29, 2020 (85 FR 32327), the EPA proposed to approve the following documents listed in Table 1 into the California SIP.

TABLE 1—SUBMITTED DOCUMENTS

Local agency	Rule or document	Adopted/ amended	Submitted
SJVUAPCD	Rule 2250—Permit-Exempt Equipment Registration	Adopted 10/19/2006	[1] 4/30/2020
SJVUAPCD	Rule 4692—Commercial Charbroiling	Amended 06/21/2018	[2] 11/21/2018
FRAQMD	Reasonably Available Control Technology (RACT) State Implementation Plan (SIP) Revision for the South Sutter County Portion of the Sacramento Metropolitan Nonattainment Area for 8-Hour ozone—Negative Declaration for Control Techniques Guidelines for the Oil and Natural Gas Industry.	Adopted 08/06/2018	[3] 12/07/2018

We proposed to approve SJVUAPCD Rule 2250 and amended Rule 4692, and FRAQMD's negative declaration for the Control Techniques Guidelines for the Oil and Natural Gas Industry (EPA–453/B–16–001), because we determined that they comply with the relevant CAA requirements. Our proposed action contains more information on the documents and our evaluation.

II. Public Comments and EPA Responses

The EPA's proposed action provided a 30-day public comment period. The public comment period closed on June 29, 2020. During this period, we received one anonymous comment that supported our proposed approval.

III. EPA Action

No comments were submitted that change our assessment of the rules and negative declaration as described in our proposed action. Therefore, as authorized in section 110(k)(3) of the Act, the EPA is fully approving the documents listed in Table 1 into the California SIP.

IV. Incorporation by Reference

In this rule, the EPA is finalizing regulatory text that includes incorporation by reference. In accordance with the requirements of 1 CFR 51.5, the EPA is finalizing the incorporation by reference of the SJVUAPCD rules described in the amendments to 40 CFR part 52 set forth below. The EPA has made, and will continue to make, these documents available through *www.regulations.gov* and at the EPA Region IX Office (please contact the person identified in the **FOR FURTHER INFORMATION CONTACT** section of this preamble for more information).

V. 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 Clean Air Act. 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 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 the 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).

In addition, the SIP is not approved to apply on any Indian reservation land or in any other area where the 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).

The Congressional Review Act, 5 U.S.C. 801 *et seq.,* as added by the Small Business Regulatory Enforcement Fairness Act of 1996, generally provides that before a rule may take effect, the agency promulgating the rule must submit a rule report, which includes a copy of the rule, to each House of the Congress and to the Comptroller General of the United States. The EPA will submit a report containing this action and other required information to the U.S. Senate, the U.S. House of Representatives, and the Comptroller General of the United States prior to publication of the rule in the **Federal Register**. A major rule cannot take effect until 60 days after it is published in the **Federal Register**. This action is not a "major rule" as defined by 5 U.S.C. 804(2).

Under section 307(b)(1) of the CAA, petitions for judicial review of this action must be filed in the United States Court of Appeals for the appropriate circuit by November 13, 2020. Filing a petition for reconsideration by the Administrator of this final rule does not affect the finality of this action for the purposes of judicial review nor does it extend the time within which a petition for judicial review may be filed, and shall not postpone the effectiveness of such rule or action. This action may not be challenged later in proceedings to

[1] This submittal was transmitted to the EPA by a letter from CARB dated April 30, 2020.

[2] This submittal was transmitted to the EPA by a letter from CARB dated November 16, 2018.

[3] This submittal was transmitted to the EPA by a letter from CARB dated December 2, 2018.

enforce its requirements. (See section 307(b)(2).)

List of Subjects in 40 CFR Part 52

Environmental protection, Air pollution control, Incorporation by reference, Intergovernmental relations, Nitrogen dioxide, Ozone, Particulate Matter, Reporting and recordkeeping requirements, Volatile organic compounds.

Dated: July 31, 2020.

John Busterud,

Regional Administrator, Region IX.

For the reasons stated in the preamble, the EPA amends Part 52, chapter I, title 40 of the Code of Federal Regulations as follows:

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 F—California

■ 2. Section 52.220 is amended by adding paragraphs (c)(310)(i)(A)(*2*) and (c)(379)(i)(C)(*8*), revising paragraph (c)(527)(i)(B) and adding paragraph (c)(540) to read as follows:

§ 52.220 Identification of plan—in part.

* * * * *

(c) * * *

(310) * * *

(i) * * *

(A) * * *

(*2*) Previously approved on June 3, 2003 in paragraph (c)(310)(i)(A)(*1*) of this section and now deleted with replacement in paragraph (c)(527)(i)(B)(*1*) of this section, Rule 4692, adopted on March 21, 2002.

* * * * *

(379) * * *

(i) * * *

(C) * * *

(*8*) Previously approved on November 3, 2011 in paragraph (c)(379)(i)(C)(*5*) of this section and now deleted with replacement in paragraph (c)(527)(i)(B)(*1*) of this section, Rule 4692, ''Commercial Charbroiling,'' amended on September 17, 2009.

* * * * *

(527) * * *

(i) * * *

(B) San Joaquin Valley Unified Air Pollution Control District.

(*1*) Rule 4692, ''Commercial Charbroiling,'' amended on June 21, 2018.

(*2*) [Reserved]

* * * * *

(540) New regulations for the following APCD were submitted on April 30, 2020, by the Governor's designee, as an attachment to a letter dated April 30, 2020.

(i) Incorporation by reference.

(A) San Joaquin Valley Unified Air Pollution Control District.

(*1*) Rule 2250, ''Permit-Exempt Equipment Registration,'' adopted October 19, 2006.

(*2*) [Reserved]

(B) [Reserved]

(ii) [Reserved]

§ 52.222 [AMENDED]

■ 3. Section 52.222 is amended by revising paragraph (a)(11) to read as follows:

(a) * * *

(11) Feather River Air Quality Management District.

(i) Negative declarations for Feather River Air Quality Management District.

CTG source category	Negative declaration CTG reference document	2006 RACT SIP submitted 7/11/07	2009 RACT SIP submitted 10/27/09	2014 RACT SIP submitted 9/29/14
Aerospace	EPA–453/R–97–004—Control of VOC Emissions from Coating Operations at Aerospace Manufacturing and Rework.	X		X
Automobile Coating; Metal Coil Container, & Closure; Paper & Fabric.	EPA–450/2–77–008—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume II Surface Coating of Cans, Coils, Paper, Fabrics, Automobiles, and Light-Duty Trucks.	X		X
Automobile and Light-Duty Truck Assembly Coatings.	EPA–453/R–08–006—Control Techniques Guidelines for Automobile and Light-Duty Assembly Coatings.		X	X
Cutback Asphalt	EPA–450/2–77–037—Control of Volatile Organic Emissions from Use of Cutback Asphalt.	X		X
Dry Cleaning	EPA–450/3–82–009—Control of Volatile Organic Compound Emissions from Large Petroleum Dry Cleaners.	X		X
Flat Wood Paneling Coatings	EPA–453/R–06–004—Control Techniques Guidelines for Flat Wood Paneling Coatings.		X	X
Fiberglass Boat Manufacturing Materials.	EPA–453/R–08–004—Control Techniques Guidelines for Fiberglass Boat Manufacturing Materials.		X	X
Flexible Package Printing	EPA–453/R06–003—Control Techniques Guidelines for Flexible Package Printing.		X	X
Gasoline Loading Terminal	EPA–450/2–77–026—Control of Hydrocarbons from Tank Truck Gasoline Loading Terminals.	X		X
Gasoline Trucks	EPA–450/2–78–051—Control of Volatile Organic Compound Leaks from Gasoline Tank Trucks and Vapor Collection Systems.	X		X
Gasoline Bulk Plants	EPA–450/2–77–035—Control of Volatile Organic Emissions from Gasoline Bulk Plants.	X		X
Graphic Arts Rotogravure and Flexography.	EPA–450/2–78–033—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume VIII: Rotogravure and Flexography.	X		X
Industrial Cleaning Solvents	EPA–453/R–06–001—Control Techniques Guidelines for Industrial Cleaning Solvents.	X	X	X

CTG source category	Negative declaration CTG reference document	2006 RACT SIP submitted 7/11/07	2009 RACT SIP submitted 10/27/09	2014 RACT SIP submitted 9/29/14
Large Appliance Coating	EPA–450/2–77–034—Control of Volatile Organic Emissions from Existing Stationary Sources, Volume V: Surface Coating of Large Appliances.	X		X
Large Appliance Coating	EPA–453/R–07–004—Control Techniques for Large Appliance Coatings.		X	X
Magnet Wire Coating	EPA–450/2–77–033—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume IV: Surface Coating of Insulation of Magnet Wire.	X		X
Metal Can Coating; Metal Coil Coating.	EPA–450/2–77–008—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume II: Surface Coating of Cans, Coils, Paper, Fabrics, Automobiles, and Light-Duty Trucks.	X		X
Metal Furniture	EPA–450/2–77–032—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume III: Surface Coating of Metal Furniture.	X		X
Metal Furniture Coatings	EPA–453/R–07–005—Control Techniques Guidelines for Metal Furniture Coatings.		X	X
Metal Parts and Products	EPA–450/2–78–015—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume VI: Surface Coating of Miscellaneous Parts and Products.	X		X
Miscellaneous Industrial Adhesives	EPA–453/R–08–005—Control Techniques Guidelines for Miscellaneous Industrial Adhesives.	X	X	X
Miscellaneous Metal and Plastic Parts Coatings.	EPA–453/R–08–003—Control Techniques Guidelines for Miscellaneous Metal and Plastic Parts Coatings.		X	X
Natural Gas/Gasoline	EPA–450/2–83–007—Control of VOC Equipment Leaks from Natural Gas/Gasoline Processing Plants.	X		X
Offset Lithographic Printing and Letterpress Printing.	EPA–453/R–06–002—Control Techniques Guidelines for Offset Lithographic Printing and Letterpress Printing.		X	X
Paper and Fabric Coating	EPA–450/2–77–008—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume II: Surface Coating of Cans, Coils, Paper, Fabrics, Automobiles, and Light-Duty Trucks.	X		X
Paper, Film, and Foil Coatings	EPA–453/R–07–003—Control Techniques Guidelines for Paper, Film, and Foil Coatings.		X	X
Petroleum Liquid Storage Tanks	EPA–450/2–77–036—Control of VOC Emissions from Storage of Petroleum Liquids in Fixed Roof Tanks.	X		X
Petroleum Liquid Storage Tanks	EPA–450/2–78–047—Control of VOC Emissions from Petroleum Liquid Storage in External Floating Roof Tanks.	X		X
Pharmaceutical Products	EPA–450/2–78–029—Control of Volatile Organic Emissions from Manufacture of Synthesized Pharmaceutical Products.	X		X
Resin Manufacturing	EPA–450/3–83–008—Control of VOC Emissions from Manufacture of High-Density Polyethylene, Polypropylene, and Polystyrene Resins.	X		X
Resin Manufacturing	EPA–450/3–83–006—Control of VOC Fugitive Emissions from Synthetic Organic Chemical Polymer and Resin Manufacturing Equipment.	X		X
Refineries	EPA–450/2–77–025—Control of Refinery Vacuum Producing Systems, Wastewater Separators, and Process Unit Turnarounds.	X		X
Refineries	EPA–450/2–78–036—Control of VOC Leaks from Petroleum Refinery Equipment.	X		X
Rubber Tire Manufacturing	EPA–450/2–78–030—Control of Volatile Organic Emissions from Manufacture of Pneumatic Rubber Tires.	X		X
Ship Coatings	61 FR 44050 Shipbuilding and Ship Repair Operations (Surface Coating).	X		X
Ship Coatings	EPA–453/R–94–032—Alternative Control Technology Document—Surface Coating Operations at Shipbuilding and Ship Repair Operations (Surface Coating).			X
Solvent Cleaning Degreasers	EPA–450/2–77–022—Control of Volatile Organic Emissions from Solvent Metal Cleaning.	X		X
Synthetic Organic Chemical Manufacturing.	EPA–450/3–84–015—Control of VOC Emissions from Air Oxidation Processes in Synthetic Organic Chemical Manufacturing Industry.	X		X

CTG source category	Negative declaration CTG reference document	2006 RACT SIP submitted 7/11/07	2009 RACT SIP submitted 10/27/09	2014 RACT SIP submitted 9/29/14
Synthetic Organic Chemical Manufacturing.	EPA–450/4–91–031—Control of VOC Emissions from Reactor Processes and Distillation Operations in Synthetic Organic Chemical Manufacturing Industry.	X	....	X
Wood Coating Factory Surface of Flat Wood Paneling.	EPA–450/2–78–032—Control of Volatile Organic Emissions from Existing Stationary Sources—Volume VII: Factory Surface of Flat Wood Paneling.	X	....	X
Wood Furniture Coating	EPA–453/R–96–007—Control of VOC Emissions from Wood Furniture Manufacturing Operations.	X	....	X

(ii) A negative declaration for the Control Techniques Guidelines for the Oil and Natural Gas Industry, EPA 453/B–16–001, was submitted on December 7, 2018, as an attachment to a letter dated December 2, 2018, and adopted on August 6, 2018, titled: ''Reasonably Available Control Technology (RACT) State Implementation Plan (SIP) Revision for the South Sutter County Portion of the Sacramento Metropolitan Nonattainment Area for 8-Hour ozone—Negative Declaration for Control Techniques Guidelines for the Oil and Natural Gas Industry.''

* * * * *

[FR Doc. 2020–17181 Filed 9–11–20; 8:45 am]

BILLING CODE 6560–50–P

NATIONAL FOUNDATION ON THE ARTS AND THE HUMANITIES

National Endowment for the Humanities

45 CFR Part 1173

RIN 3136–AA42

Processes and Procedures for Issuing Guidance Documents

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

ACTION: Final rule.

SUMMARY: This final rule sets forth the National Endowment for the Humanities' (NEH) internal policies and procedures governing the issuance of guidance documents as required by Executive Order 13891, ''Promoting the Rule of Law Through Improved Agency Guidance Documents'' (E.O. 13891).

DATES: This final rule is effective on October 14, 2020.

FOR FURTHER INFORMATION CONTACT: Lisette Voyatzis, Deputy General Counsel, 400 7th Street SW, Room 4060, Washington, DC 20506; (202) 606–8322; *gencounsel@neh.gov.*

SUPPLEMENTARY INFORMATION:

1. Background

NEH is adopting this final rule pursuant to E.O. 13891,[1] which requires federal agencies to finalize regulations, or amend existing regulations as necessary, that set forth processes and procedures for issuing guidance documents. In compliance with E.O. 13891, this final rule establishes NEH's policy, procedures, and responsibilities for issuing guidance documents in order to ensure that the agency performs the required review and clearance before issuance and follows all stages of the rulemaking process.

2. Compliance

Administrative Procedure Act of 1946

Under the Administrative Procedure Act, an agency may waive the normal notice and comment procedures if the action is a rule of agency organization, procedure, or practice. *See* 5 U.S.C. 553(b)(A). This final rule merely incorporates the requirements set forth in E.O. 13891 into NEH's internal policy and procedures for issuing guidance documents. Accordingly, NEH has concluded that there is good cause to publish this rule without prior public notice and comment.

E.O. 12866, Regulatory Planning and Review, and E.O. 13563, Improving Regulation and Regulatory Review

This action is not significant under E.O. 12866.

E.O. 13771, Reducing Regulation and Controlling Regulatory Costs

This action is not expected to be an E.O. 13771 regulatory action because this action is not significant under E.O. 12866.

E.O. 13132, Federalism

This rulemaking does not have federalism implications. It will 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.

E.O. 12988, Civil Justice Reform

This rulemaking 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.

E.O. 13175, Indian Tribal Governments

Under the criteria in E.O. 13175, NEH evaluated this final rule and determined that it will not have any potential effects on Federally recognized Indian Tribes.

E.O. 12630, Takings

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

Regulatory Flexibility Act of 1980

This rulemaking 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

This rulemaking does not impose an information collection burden under the Paperwork Reduction Act. This action contains no provisions constituting a collection of information pursuant to the Paperwork Reduction Act.

Unfunded Mandates Reform Act of 1995

This rulemaking 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

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

[1] 84 FR 55235 (Oct. 9, 2019).

Small Business Regulatory Enforcement Fairness Act of 1996

This action pertains to agency management, personnel, and organization and does not substantially affect the rights or obligations of nonagency parties. Accordingly, it is not a ''rule'' as that term is used by the Congressional Review Act (Subtitle E of the Small Business Regulatory Enforcement Fairness Act of 1996), and the reporting requirement of 5 U.S.C. 801 does not apply.

E-Government Act of 2002

All information about NEH required to be published in the **Federal Register** may be accessed at *www.neh.gov.* The website *https://www.regulations.gov* contains electronic dockets for NEH's rulemakings under the Administrative Procedure Act of 1946.

Plain Writing Act of 2010

To ensure this final rule was written in plain and clear language so that it can be used and understood by the public, NEH modeled the language of this final rule on the Federal Plain Language Guidelines.

List of Subjects in 45 CFR 1173

Administrative practice and procedure.

■ For the reasons stated in the preamble, the National Endowment for the Humanities adds 45 CFR part 1173 to read as follows:

PART 1173—PROCESSES AND PROCEDURES FOR ISSUING GUIDANCE DOCUMENTS

Sec.
1173.1 Purpose and scope.
1173.2 Definition of guidance document.
1173.3 Review and clearance.
1173.4 Requirements for clearance.
1173.5 Public access to guidance documents.
1173.6 Waiver of publication of guidance documents.
1173.7 Good faith cost estimates.
1173.8 Definition of significant guidance document.
1173.9 Procedures for significant guidance documents.
1173.10 Notice-and-comment procedures.
1173.11 Petitions to withdraw or modify guidance.
1173.12 Rescinded guidance.
1173.13 Exigent circumstances.
1173.14 Reports to Congress and the Government Accountability Office (GAO).
1173.15 No judicial review or enforceable rights.

Authority: 5 U.S.C. 301; 20 U.S.C. 956.

§ 1173.1 Purpose and scope.

(a) This part prescribes general procedures that apply to guidance documents issued by the National Endowment for the Humanities (NEH).

(b) This part governs all NEH employees and contractors (collectively, NEH staff) involved with all phases of issuing NEH guidance documents.

(c) This part applies to all NEH guidance documents in effect on or after October 14, 2020.

§ 1173.2 Definition of guidance document.

(a) For purposes of this part, the term guidance document means any agency statement of general applicability, intended to have future effect on the behavior of regulated parties, that sets forth a policy on a statutory, regulatory, or technical issue, or an interpretation of a statute or regulation, but does not include the following:

(1) Rules promulgated pursuant to notice and comment under 5 U.S.C. 553 or similar statutory provisions;

(2) Rules exempt from rulemaking requirements under 5 U.S.C. 553(a);

(3) Rules of agency organization, procedure, or practice;

(4) Decisions of agency adjudications under 5 U.S.C. 554 or similar statutory provisions;

(5) Internal guidance directed to the issuing agency or other agencies that is not intended to have substantial future effect on the behavior of regulated parties;

(6) Internal executive branch legal advice or legal opinions addressed to executive branch officials;

(7) Agency statements of specific applicability, including advisory or legal opinions directed to particular parties about circumstance-specific questions (*e.g.,* case or investigatory letters responding to complaints, warning letters), notices regarding particular locations or facilities (*e.g.,* guidance pertaining to the use, operation, or control of a government facility or property), and correspondence with individual persons or entities (*e.g.,* congressional correspondence), except documents ostensibly directed to a particular party but designed to guide the conduct of the broader regulated public;

(8) Legal briefs, other court filings, or positions taken in litigation or enforcement actions;

(9) Agency statements that do not set forth a policy on a statutory, regulatory, or technical issue or an interpretation of a statute or regulation, including speeches and individual presentations, editorials, media interviews, press materials, or congressional testimony that do not set forth for the first time a new regulatory policy;

(10) Guidance pertaining to military or foreign affairs functions;

(11) Grant solicitations and awards;

(12) Contract solicitations and awards; or

(13) Purely internal agency policies or guidance directed solely to NEH staff or other federal agencies that are not intended to have substantial future effect on the behavior of regulated parties.

§ 1173.3 Review and clearance.

All NEH guidance documents, as defined in § 1173.2, require review and clearance in accordance with this part. All agency guidance documents must be reviewed and cleared by NEH's Office of the General Counsel (OGC).

§ 1173.4 Requirements for clearance.

The NEH OGC's review and clearance of guidance documents shall ensure that each guidance document the agency proposes to issue satisfies the following requirements:

(a) The guidance document complies with all relevant statutes and regulations (including any statutory deadlines for agency action);

(b) The guidance document identifies or includes:

(1) The term ''guidance'' or its functional equivalent;

(2) A concise name for the guidance document;

(3) The NEH office or division issuing the guidance document;

(4) A unique identifier, including, at a minimum, the date of issuance, title of the document, and a number assigned by NEH's OGC (or, in the case of a significant guidance document, the Z–RIN (regulatory identification number));

(5) The general topic that the guidance document addresses;

(6) Citations to applicable statutes and regulations;

(7) A statement noting whether the guidance is intended to revise or replace any previously issued guidance and, if so, sufficient information to identify the previously issued guidance; and

(8) A concise summary of the guidance document's content.

(c) The guidance document avoids using mandatory language, such as ''shall,'' ''must,'' ''required,'' or ''requirement,'' unless the language is describing an established statutory or regulatory requirement or is addressed to NEH staff and will not foreclose NEH's consideration of positions advanced by affected private parties;

(d) The guidance document is written in plain and understandable English; and

(e) All guidance documents include a clear and prominent statement declaring that the contents of the document do not have the force and effect of law, are not meant to bind the public in any way, and the document is intended only to provide clarity to the public regarding existing requirements under the law or NEH's policies.

§ 1173.5 Public access to guidance documents.

NEH will:

(a) Oversee the creation of a guidance portal on the agency's website;

(b) Ensure all effective guidance documents, identified by a unique identifier as described in § 1173.4(b)(4), are on the guidance portal in a single, searchable, indexed database, and available to the public;

(c) Note on the agency's guidance portal that guidance documents lack the force and effect of law, except as authorized by law or as incorporated into a contract;

(d) Maintain and publish on NEH's guidance portal a means for the public to comment electronically on any guidance documents that are subject to notice-and-comment procedures, and to submit requests electronically for issuance, reconsideration, modification, or rescission of guidance documents in accordance with § 1173.11;

(e) Include on the agency's guidance portal the date on which all guidance documents were posted to the website and a hyperlink to all guidance documents;

(f) Receive and address complaints from the public that NEH is not following the requirements of OMB's Good Guidance Bulletin or that NEH is improperly treating a guidance document as a binding requirement;

(g) Note on the agency's guidance portal that any guidance document not posted on the guidance portal is rescinded, and that neither the agency nor a party may cite, use, or rely on any guidance document that is not posted on the guidance portal, except to establish historical facts; and

(h) Include a link to this part on the agency's guidance portal.

§ 1173.6 Waiver of publication of guidance documents.

(a) Sections 1173.5(b) and (e) do not apply to guidance documents for which a waiver has been applied from the OMB Director pursuant to Subsection 3(c) of Executive Order (E.O.) 13891.

(b) Requests for waivers must be written and signed by a senior policy official at the agency.

§ 1173.7 Good faith cost estimates.

(a) NEH will, to the extent practicable, make a good faith effort to estimate the likely economic cost impact of the guidance document to determine whether the document might be significant.

(b) When assessing or explaining whether it believes a guidance document is significant, NEH will, at a minimum, provide the same level of analysis that would be required for a major determination under the Congressional Review Act.[2]

(c) When OMB's Office of Information and Regulatory Affairs (OIRA) determines that a guidance document will be economically significant, NEH will conduct and publish an assessment of the potential costs and benefits of the regulatory action (which may entail a regulatory impact analysis) of the sort that would accompany an economically significant rulemaking, to the extent reasonably possible.

§ 1173.8 Definition of significant guidance document.

(a) The term *significant guidance document* means a guidance document that will be disseminated to regulated entities or the general public and that may reasonably be anticipated:

(1) To lead to an annual effect on the economy of $100 million or more or adversely affect in a material way the United States economy, a sector of the United States economy, productivity, competition, jobs, the environment, public health or safety, or state, local, or tribal governments or communities;

(2) To create serious inconsistency or otherwise interfere with an action that another federal agency has taken or planned;

(3) To alter materially the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or

(4) To raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in E.O. 12866, as further amended.

(b) The term significant guidance document does not include the categories of documents excluded by this part or any other category of guidance documents that NEH's OGC, in consultation with OIRA, has exempted in writing.

§ 1173.9 Procedures for significant guidance documents.

(a) NEH will make an initial, preliminary determination about a guidance document's significance. Thereafter, NEH will submit the document to OIRA to determine whether a guidance document is significant, unless the guidance is otherwise exempted from such a determination by the Administrator of OIRA.

(b) If OIRA designates a guidance document as significant, NEH will submit the guidance document to OIRA for review under E.O. 12866 prior to issuing it; and NEH will process significant guidance in compliance with the applicable requirements for regulations or rules, including significant regulatory actions, as set forth in E.O. 12866, E.O. 13563, E.O. 13609, E.O. 13771, and E.O. 13777.

(c) The NEH Chairperson signs or approves significant guidance documents.

§ 1173.10 Notice-and-comment procedures.

Except as provided in paragraph (b) of this section, all proposed NEH guidance documents determined to be significant guidance documents within the meaning of § 1173.8 will be subject to the following informal notice-and-comment procedures.

(a) NEH's OGC will:

(1) Publish a notice in the **Federal Register** announcing that a draft of the proposed guidance document is publicly available;

(2) Post the draft guidance document on its website, at *www.neh.gov/guidance;*

(3) Invite public comment on the draft document for a minimum of thirty (30) days; and

(4) Prepare and post a public response to major concerns raised in the comments, as appropriate, on its guidance portal, either before or when the guidance document is finalized and issued.

(b) The requirements of paragraph (a) of this section will not apply to any significant guidance documents or categories of significant guidance documents for which NEH's OGC finds—in consultation with OIRA, the proposing NEH office/division, and the NEH Chairperson—good cause that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest (and incorporates the finding of good cause and a brief statement of reasons therefor in the issued guidance).

(c) Where appropriate, NEH's OGC may recommend to the NEH Chairperson that a particular guidance document that is otherwise of importance to the agency's interests should also be subject to the informal notice-and-comment procedures described in paragraph (a) of this section.

[2] See OMB Memorandum M–19–14, Guidance on Compliance with the Congressional Review Act (April 11, 2019).

§ 1173.11 Petitions to withdraw or modify guidance.

(a) Any person may submit a petition to NEH requesting withdrawal or modification of any effective guidance document by writing to the NEH Office of the General Counsel at: *gencounsel@neh.gov,* or National Endowment for the Humanities, Attn: Office of the General Counsel, 400 Seventh Street SW, Washington, DC 20506.

(b) The petition must:

(1) Describe the nature of the request and provide the title or substance of the guidance you are requesting that NEH withdraw or modify; and

(2) Explain, with justification, how the document should be modified or why the document should be withdrawn.

(c) NEH will review each request and determine whether to grant the request or deny it in whole or in part. NEH will respond to all requests in a timely manner, but no later than ninety (90) days after receipt of the request.

§ 1173.12 Rescinded guidance.

(a) NEH's OGC, in consultation with the NEH office/division that issued the guidance document, shall determine whether to rescind a guidance document.

(b) Once rescinded, NEH will remove the hyperlink to the guidance document from the guidance portal. The agency will list on the guidance portal, for at least one year after rescission, the guidance document's name, title, unique identifier, and date of rescission.

(c) No NEH office/division or NEH staff may cite, use, or rely on guidance documents that are rescinded, except to establish historical facts.

§ 1173.13 Exigent circumstances.

In emergency situations, or when NEH is required by statutory deadline or court order to act more quickly than normal review procedures allow, NEH will notify OIRA as soon as possible and, to the extent practicable, comply with the requirements of this part at the earliest opportunity. Wherever practicable, NEH should schedule its proceedings to permit sufficient time to comply with the procedures set forth in this part.

§ 1173.14 Reports to Congress and the Government Accountability Office (GAO).

Unless otherwise determined in writing, NEH will, upon issuing a guidance document, submit a report to Congress and GAO in accordance with the procedures described in the Congressional Review Act.

§ 1173.15 No judicial review or enforceable rights.

This part is intended to improve the internal management of the National Endowment for the Humanities. As such, it is for the use of NEH personnel only and is not intended to, and does not, create any right or benefit, substantive or procedural, enforceable at law or in equity by any party against the United States, its agencies or other entities, its officers or employees, or any other person.

Dated: August 18, 2020.

Caitlin Cater,

Attorney-Advisor, National Endowment for the Humanities.

[FR Doc. 2020–18481 Filed 9–11–20; 8:45 am]

BILLING CODE 7536–01–P

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Part 54

[WC Docket Nos. 19–126, 10–90; FCC 20–5; FRS 16999]

Rural Digital Opportunity Fund, Connect America Fund

AGENCY: Federal Communications Commission.

ACTION: Final rule; announcement of effective date.

SUMMARY: In this document, the Federal Communications Commission (Commission) announces that the Office of Management and Budget (OMB) has approved, for a period of three years, an information collection associated with the rules for the Connect America Fund Phase II and Rural Digital Opportunity Fund auctions contained in the Commission's *Rural Digital Opportunity Fund Order,* FCC 20–5. This document is consistent with the *Rural Digital Opportunity Fund Order,* which stated that the Commission would publish a document in the **Federal Register** announcing the effective date of the new information collection requirements.

DATES: The amendments to § 54.804(b) and (c) published at 85 FR 13773, March 10, 2020 are effective September 14, 2020.

FOR FURTHER INFORMATION CONTACT: Alexander Minard, Wireline Competition Bureau at (202) 418–7400 or TTY (202) 418–0484. For additional information concerning the Paperwork Reduction Act information collection requirements contact Nicole Ongele at (202) 418–2991 or via email at *Nicole.Ongele@fcc.gov.*

SUPPLEMENTARY INFORMATION: The Commission submitted revised information collection requirements for review and approval by OMB, as required by the Paperwork Reduction Act (PRA) of 1995, on June 22, 2020. OMB approved the new information collection requirements on August 4, 2020. The information collection requirements are contained in the Commission's *Rural Digital Opportunity Fund Order,* FCC 20–5, published at 85 FR 13773, March 10, 2020. The OMB Control Number is 3060–1256. The Commission publishes this document as an announcement of the effective date of the rules published on March 10, 2020. If you have any comments on the burden estimates listed in the following, or how the Commission can improve the collections and reduce any burdens caused thereby, please contact Nicole Ongele, Federal Communications Commission, Room 1–A620, 445 12th Street SW, Washington, DC 20554. Please include the OMB Control Number, 3060–1256, in your correspondence. The Commission will also accept your comments via email at *PRA@fcc.gov.* 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), (202) 418–0432 (TTY).

Synopsis

As required by the Paperwork Reduction Act of 1995 (44 U.S.C. 3507), the Commission is notifying the public that it received OMB approval on August 4, 2020, for the information collection requirements contained in 47 CFR 54.804(b) and (c) published at 85 FR 13773, March 10, 2020. Under 5 CFR part 1320, an agency may not conduct or sponsor a collection of information unless it displays a current, valid OMB Control Number. No person shall be subject to any penalty for failing to comply with a collection of information subject to the Paperwork Reduction Act that does not display a current, valid OMB Control Number. The OMB Control Number is 3060–1256. The foregoing notice is required by the Paperwork Reduction Act of 1995, Public Law 104–13, October 1, 1995, and 44 U.S.C. 3507.

The total annual reporting burdens and costs for the respondents are as follows:

OMB Control Number: 3060–1256.

OMB Approval Date: August 4, 2020.

OMB Expiration Date: August 31, 2023.

Title: Application for Connect America Fund Phase II and Rural Digital Opportunity Fund Auction Support.

Form Number: FCC Form 683.

Type of Review: Revision of a currently approved collection.

Respondents: Business or other for-profit entities, Not-for-profit institutions, and State, Local or Tribal Governments.

Number of Respondents and Responses: 530 respondents; 1,060 responses.

Estimated Time per Response: 2–12 hours (on average).

Frequency of Response: Annual reporting requirements, on occasion reporting requirement.

Obligation to Respond: Required to obtain or retain benefits. Statutory authority for this information collection 47 U.S.C. 154, 214, 254 and 303(r) of the Communications Act of 1934, as amended.

Total Annual Burden: 7,420 hours.

Total Annual Cost(s): No cost.

Nature and Extent of Confidentiality: Although most information collected in FCC Form 683 will be made available for public inspection, the Commission will withhold certain information collected in FCC Form 683 from routine public inspection. Specifically, the Commission will treat certain financial and technical information submitted in FCC Form 683 as confidential. In addition, an applicant may use the abbreviated process under 47 CFR 0.459(a)(4) to request confidential treatment of the audited financial statements that are submitted during the post-selection review process. However, if a request for public inspection for this technical or financial information is made under 47 CFR 0.461, and the applicant has any objections to disclosure, the applicant will be notified and will be required to justify continued confidential treatment. To the extent that an applicant seeks to have other information collected in FCC Form 683 or during the post-selection review process withheld from public inspection, the applicant may request confidential treatment pursuant to 47 CFR 0.459.

Privacy Act Impact Assessment: No impact(s).

Needs and Uses

Connect America Fund Phase II Auction

On November 18, 2011, the Commission released the *USF/ICC Transformation Order and Further Notice of Proposed Rulemaking,* WC Docket No. 10–90 et al., FCC 11–161 (*USF/ICC Transformation Order and/or FNPRM*), which comprehensively reformed and modernized the high-cost program within the universal service fund to focus support on networks capable of providing voice and broadband services. Among other things, the Commission created the Connect America Fund (CAF) and concluded that support in price cap areas would be provided through a combination of ''a new forward-looking model of the cost of constructing modern multi-purpose networks'' and a competitive bidding process (CAF Phase II auction or Auction 903). The Commission also sought comment in the accompanying *USF/ICC Transformation FNPRM* on proposed rules governing the CAF Phase II auction, including basic auction design and the application process.

In the CAF Phase II auction, service providers competed to receive support of up to $1.98 billion over 10 years to offer voice and broadband service in unserved high-cost areas. The information collection requirements reported under this collection are the result of several Commission decisions to implement the reform adopted in the *USF/ICC Transformation Order* and move forward with conducting the CAF Phase II auction. In the *April 2014 Connect America Order,* WC Docket No. 10–90 et al., FCC 14–54, the Commission adopted various rules regarding participation in the CAF Phase II auction, the term of support, and the eligible telecommunications carrier (ETC) designation process. In the *Phase II Auction Order,* WC Docket No. 10–90 et al., FCC 16–64, the Commission adopted rules to govern the CAF Phase II auction, including the adoption of a two-stage application process, which includes a pre-auction short-form application to be submitted by parties interested in bidding in the CAF Phase II auction and a post-auction long-form application that must be submitted by winning bidders seeking to become authorized to receive CAF Phase II auction support. The Commission concluded, based on its experience with auctions and consistent with the record, that this two-stage application process balances the need to collect information essential to conducting a successful auction and authorizing CAF Phase II support with administrative efficiency.

On January 30, 2018, the Commission adopted a public notice that established the final procedures for the CAF Phase II auction, including the long-form application disclosure and certification requirements for winning bidders seeking to become authorized to receive CAF Phase II auction support. *See Phase II Auction Procedures Public Notice,* WC Docket No. 17–182 et al., FCC 18–6. The Commission also adopted the *Phase II Auction Order on Reconsideration,* WC Docket No. 10–90 et al., FCC 18–5, which modified the Commission's letter of credit rules to provide some additional relief for CAF Phase II auction support recipients by reducing the costs of maintaining a letter of credit.

The Commission reduces the number of respondents that are subject to this collection now that the CAF Phase II auction winning bidders have been announced.

Rural Digital Opportunity Fund Auction

On February 7, 2020 the Commission released the *Rural Digital Opportunity Fund Order,* WC Docket Nos. 19–126, 10–90, FCC 20–5 which will commit up to $20.4 billion over the next decade to support up to gigabit speed broadband networks in rural America. The funding will be allocated through a multi-round, reverse, descending clock auction that favors faster services with lower latency and encourages intermodal competition in order to ensure that the greatest possible number of Americans will be connected to the best possible networks, all at a competitive cost.

To implement the Rural Digital Opportunity Fund auction, the Commission adopted new rules for the Rural Digital Opportunity Fund auction, including the adoption of a two-stage application process. Like with the CAF Phase II auction, this process includes a pre-auction short-form application to be submitted by parties interested in bidding in the Rural Digital Opportunity Fund auction (FCC Form 183) and a post-auction long-form application that must be submitted by winning bidders (or their designees) seeking to become authorized to receive Rural Digital Opportunity Fund support (FCC Form 683). The Commission received approval for the short-form application (FCC Form 183) in a separate collection under the OMB control number 3060–1252.

The Commission plans to submit at a later date additional revisions or new collections for OMB review to address other reforms adopted in the above-referenced Order.

The Commission therefore revises this information collection to reflect these requirements to determine the recipients of Connect America Phase II auction and Rural Digital Opportunity Fund auction support.

Federal Communications Commission.

Marlene Dortch,

Secretary, Office of the Secretary.

[FR Doc. 2020–17728 Filed 9–11–20; 8:45 am]

BILLING CODE 6712–01–P

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Part 64

[CG Docket No. 17–59; FCC 20–96; FRS 16971]

Advanced Methods To Target and Eliminate Unlawful Robocalls

AGENCY: Federal Communications Commission.

ACTION: Final rule.

SUMMARY: In this document, the Commission adopts two safe harbors for voice service providers that block calls in certain situations, and adopts certain measures to ensure that erroneous blocking is quickly remedied. Specifically, the Commission adopts a safe harbor from liability under the Communications Act and the Commission's rules for terminating voice service providers that block calls on an opt-out basis based on reasonable analytics designed to identify unwanted calls, so long as those take into account information provided by caller ID authentication where available for a particular call. Second, the Commission adopts a safe harbor enabling voice service providers to block traffic from bad-actor upstream voice service providers that continue to allow unwanted calls to traverse their networks. Finally, the Commission requires that blocking providers furnish a single point of contact to resolve unintended or inadvertent blocking, and emphasizes that, when blocking, they should make all reasonable efforts to ensure that critical calls, such as those from Public Safety Answering Points (PSAPs), are not blocked and that they should never block calls to 911. These rules both respond to voice service providers that seek assurance that their good-faith blocking will not result in liability if they inadvertently block wanted calls and implement the call blocking provisions of the TRACED Act, and provide safeguards against erroneous blocking.

DATES: Effective October 14, 2020.

FOR FURTHER INFORMATION CONTACT: Jerusha Burnett, Consumer Policy Division, Consumer and Governmental Affairs Bureau, email at *jerusha.burnett@fcc.gov* or by phone at (202) 418–0526.

SUPPLEMENTARY INFORMATION: This is a summary of the Commission's *Report and Order,* in CG Docket No. 17–59, FCC 20–96, adopted on July 16, 2020, and released on July 17, 2020. The *Further Notice of Proposed Rulemaking* that was adopted concurrently with the *Report and Order* published July 31, 2020 at 85 FR 46063. The full text of document FCC 20–96 is available for public inspection and copying via the Commission's Electronic Comment Filing System (ECFS). The full text of document FCC 20–96 and any subsequently filed documents in this matter may also be found by searching ECFS at: *http://apps.fcc.gov/ecfs/* (insert CG Docket No. 17–59 into the Proceeding block). 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).

Final Paperwork Reduction Act of 1995 Analysis

The *Report and Order* does not contain any new or modified information collection requirements subject to the Paperwork Reduction Act of 1995, Public Law 104–13. It, therefore, does not contain any new or modified information collection burden for small business concerns with fewer than 25 employees, pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107–198, *see* 44 U.S.C. 3506(c)(4).

Congressional Review Act

The Commission sent a copy of the *Report and Order* to Congress and the Government Accountability Office pursuant to the Congressional Review Act, *see* 5 U.S.C. 801(a)(1)(A).

Synopsis

1. With the *Report and Order,* the Commission takes specific and concrete steps to further protect consumers against unwanted calls. The Commission adopts a safe harbor from liability under the Communications Act and its rules for terminating voice service providers that block calls based on reasonable analytics designed to identify unwanted calls, so long as those take into account information provided by STIR/SHAKEN (or, for non-IP based calls, any other effective call authentication framework that satisfies the Pallone-Thune Telephone Robocall Abuse Criminal Enforcement And Deterrence (TRACED) Act) when such information is available for a particular call. And the Commission establishes a second safe harbor enabling voice service providers to block traffic from bad-actor upstream voice service providers that continue to allow unwanted calls to traverse their networks. Finally, the Commission requires that blocking providers furnish a single point of contact to resolve unintended or inadvertent blocking, and emphasizes that, when blocking, they should make all reasonable efforts to ensure that critical calls, such as those from PSAPs, are not blocked and that they should never block calls to 911.

Safe Harbors

2. Consistent with the TRACED Act and in light of the record garnered in response to the Commission's *Call Blocking Declaratory Ruling and Further Notice,* the Commission adopts two safe harbors from liability under the Communications Act and the Commission's rules for certain call blocking by voice service providers. The first is a call-by-call safe harbor based on reasonable analytics including caller ID authentication information. The second safe harbor targets bad-actor upstream voice service providers who do not police their networks to minimize bad traffic after being notified of such traffic.

3. *Scope of Safe Harbor Protection.* The safe harbors the Commission establishes here will protect blocking providers from liability arising from any obligations related to completing the call under the Communications Act and the Commission's rules.

Safe Harbor Based on Reasonable Analytics

4. First, the Commission adopts a safe harbor from liability under the Communications Act and the Commission's rules for the unintended or inadvertent blocking of wanted calls where terminating voice service providers block based on reasonable analytics that include caller ID authentication information and the consumer is given the opportunity to opt out. Consistent with the Commission's statement in the *Call Blocking Declaratory Ruling,* published at 84 FR 29387, June 24, 2019, *and Further Notice (NPRM),* published at 84 FR 29478, June 24, 2019; and Congress' guidance in the TRACED Act, the Commission requires terminating voice service providers that take advantage of this safe harbor to offer these services without a line-item charge to consumers.

5. *Caller ID Authentication Requirement.* To avail themselves of the safe harbor, terminating voice service providers must incorporate caller ID authentication information into their reasonable analytics programs. At this time, only the STIR/SHAKEN caller ID authentication framework satisfies this requirement. As the Commission explains, however, should it later identify other effective caller ID authentication methods that would

satisfy the TRACED Act, including non-IP methods, those methods would also satisfy its requirements here.

6. At a minimum, a terminating voice service provider seeking safe harbor protection must have deployed an effective caller ID authentication framework within their own network, accept caller ID authentication information transmitted by an upstream voice service provider, and incorporate that information into its analytics where that information is available. The terminating voice service provider may also rely on this safe harbor even when blocking calls where caller ID authentication information is not available, so long as it incorporates caller ID authentication information into its analytics wherever possible.

7. In recognition of commenter concerns, and of the need to adapt to evolving threats, the Commission gives terminating voice service providers flexibility in how to incorporate authentication into their analytics. They may, for example, take into account the level of attestation, including looking at what level of attestation has historically been present where such data is available. The Commission reiterates that voice service providers must apply analytics reasonably in a non-discriminatory, competitively neutral manner.

8. The TRACED Act acknowledges that voice service providers' ability to deploy STIR/SHAKEN varies because, in part, it is not designed to work on non-IP networks. As a result, this requirement means that terminating voice service providers with exclusively non-IP based networks will not be able to avail themselves of the safe harbor immediately. Should industry develop alternative caller ID authentication technologies that it later determines satisfy this requirement under the TRACED Act, those technologies would also be sufficient to claim the safe harbor. Further, the Commission recognizes that all terminating voice service providers are likely to receive calls from upstream voice service providers with non-IP networks. If a portion of the calls received by the terminating voice service provider are authenticated and the terminating voice service provider is verifying those calls and incorporating that information into a program of reasonable analytics, the safe harbor would still be available for the blocking of calls from non-IP networks. Limiting the safe harbor to authenticated calls could encourage bad actors to ensure that their calls originate or transit on non-IP networks, undermining the value of the safe harbor.

Safe Harbor for Blocking of Bad-Actor Providers

9. The Commission clarifies that voice service providers may block calls from certain bad-actor upstream voice service providers and establishes a safe harbor from liability related to call completion obligations arising under the Communications Act and the Commission's rules for this blocking. Unlike the reasonable analytics safe harbor, the Commission focuses here on criteria that clearly indicate a particular upstream voice service provider is facilitating, or at a minimum shielding, parties originating illegal calls.

10. *Permitting Provider-Based Blocking.* Until very recently, the Commission has only authorized call blocking for particular calls, not based on the provider. Here, the Commission clarifies that voice service providers are permitted to block calls from ''bad-actor'' upstream voice service providers. Specifically, the Commission makes clear that a voice service provider may block calls from an upstream voice service provider that, when notified that it is carrying bad traffic by the Commission, fails to effectively mitigate such traffic or fails to implement effective measures to prevent new and renewing customers from using its network to originate illegal calls. The notification from the Commission will be based on information obtained through traceback, likely in coordination with the Traceback Consortium. Failure of the bad-actor provider to sign calls may be an additional factor in this notification.

11. *Notification and Effective Mitigation Measures.* If the Commission identifies illegal traffic on the network, it may notify the voice service provider that it is passing identified bad traffic and that specific calls are illegal. Upon receipt of this notification, the voice service provider should promptly investigate and, if necessary, prevent the illegal caller from continuing to use the network to place illegal calls. If the upstream voice service provider fails to take effective mitigation measures within 48 hours, a voice service provider may then, after notifying the Commission as discussed below, block calls from this bad-actor provider. Similarly, if the upstream voice service provider fails to implement effective measures to prevent new and renewing customers from using its network to originate illegal calls, a voice service provider may also block calls from this bad-actor provider.

12. A notified voice service provider should inform the Commission and the Traceback Consortium within 48 hours of steps it has taken to mitigate the illegal traffic. A voice service provider that is aware of the notice provided to an upstream voice service provider must consider whether the steps taken were sufficient to effectively mitigate the identified bad traffic. The Commission declines to mandate specific metrics to make this determination, but expects that they will generally involve a significant reduction in the traffic stemming from a particular illegal calling campaign or regarding calls from the particular upstream voice service provider. The voice service provider may meet this criterion if it determines, in good faith and upon a rational basis, that the upstream voice service provider has failed to effectively mitigate the illegal traffic. The Commission expects the voice service provider to inform the upstream voice service provider of that determination in order to give the upstream voice service provider another opportunity to take further mitigation steps. In addition, before taking any action to block calls of the upstream voice service provider, a voice service provider must provide the Commission with notice and a brief summary of its basis for making such a determination. By obtaining such information from both parties, the Commission will be in a position to monitor the actions of both parties prior to commencement of any blocking.

13. A notified voice service provider should also inform the Commission and the Traceback Consortium within a reasonable period of time of the steps it takes to prevent new and renewing customers from originating illegal calls. Failure to provide this information within a reasonable time shall be equivalent to having failed to have effective measures in place for purposes of the safe harbor. Where upstream voice service providers disclose their measures, a voice service provider may in good faith assess whether the measures are effective based on objective criteria, such as whether customers can show a legitimate business need for those services. Again, before taking any action to block calls of the upstream voice service provider, a voice service provider must provide the Commission with notice and a brief summary of its basis for making such a determination.

14. *Risk of Legal Calls Being Blocked.* The Commission finds that the benefits of this safe harbor outweigh the potential costs of blocking some legal calls in the process. Voice service providers are in the best position to detect and combat this problem. Accordingly, the Commission believes that enabling voice service providers to

use all available technologies and methodologies at their disposal without fear of liability is crucial to combat illegal calls. This safe harbor encourages voice service providers to both mitigate bad traffic once they have actual notice of that traffic, and to take proactive steps to prevent their networks from being used to transmit illegal calls.

Protections Against Erroneous Blocking

15. *Protections for Critical Calls.* The Commission requires that all voice service providers must make all reasonable efforts to ensure that calls from PSAPs and government outbound emergency numbers are not blocked.

16. Calls to PSAPs via 911 are also extremely important and the Commission makes clear that they should never be blocked unless the voice service provider knows without a doubt that the calls are unlawful. Though some unwanted and illegal calls may reach 911 call centers, the Commission believes that 911 call centers themselves are best equipped to determine how to handle the calls they receive.

17. *Point of Contact for Blocking Disputes.* The Commission requires that any voice service provider that blocks calls must designate a single point of contact for callers, as well as other voice service providers, to report blocking errors at no charge to callers or other voice service providers.

18. Blocking providers must investigate and resolve these blocking disputes in a reasonable amount of time and at no cost to the caller, so long as the complaint is made in good faith. What amount of time is ''reasonable'' may vary depending on the specific circumstances of the blocking and the resolution of the blocking dispute, and pending further developments in the record Blocking providers must also publish contact information clearly and conspicuously on their public-facing websites. The Commission further requires that when a caller makes a credible claim of erroneous blocking and the voice service provider determines that the calls should not have been blocked, a voice service provider must promptly cease blocking calls from that number unless circumstances change. Finally, because the TRACED Act requires that the establishment of a safe harbor be consistent with the Act's requirement of ''transparency and effective redress options,'' the Commission confirms that implementation of these redress mechanisms is a condition of obtaining the protections of the safe harbors it establishes in the *Report and Order.*

19. Consistent with what the Commission permitted in June 2019, consumers may choose, either via opt in or opt out consent, to have their terminating voice service provider block categories of calls that may include legal calls. In these cases, terminating voice service providers are not obliged to cease blocking such calls merely because the caller claims they are legal. Rather, a terminating voice service provider's analysis should hinge on whether the disputed calls fit within the blocking categories to which their customers have consented.

20. *No Critical Calls List at this Time.* The Commission declines to adopt a Critical Calls List at this time, in light of a record largely in opposition and in recognition that such a list would likely to do more harm than good. The Commission does not, however, foreclose the possibility of adopting such a list at a future point in time should circumstances change.

Final Regulatory Flexibility Analysis

21. As required by the Regulatory Flexibility Act of 1980 (RFA), as amended, an Initial Regulatory Flexibility Analysis (IRFA) was incorporated into the *Declaratory Ruling and Further Notice.* The Commission sought written public comment on the proposals in the *NPRM,* including comment on the IRFA. The comments received are discussed below. The Final Regulatory Flexibility Analysis (FRFA) conforms to the RFA.

Need for, and Objectives of, the Order

22. The *Report and Order* takes important steps in the fight against illegal robocalls by enabling terminating voice service providers to block certain calls before they reach consumers' phones while also requiring certain protections for lawful calls. The rules the Commission adopts today outline two safe harbors for terminating voice service providers that block calls in these circumstances. First, the *Report and Order* establishes a safe harbor for terminating voice service providers that block calls on a default, opt-out, basis based on reasonable analytics so long as those analytics include caller ID authentication information and the customer is given sufficient information to make an informed choice. Second, it establishes a safe harbor for voice service providers that block and then cease accepting all traffic from an upstream voice service provider that, when notified that it is carrying bad traffic by the Commission, fails to effectively mitigate such traffic or fails to implement effective measures to prevent new and renewing customers from using its network to originate illegal calls. The *Report and Order* also adopts rules to ensure that callers and other voice service providers can resolve potential erroneous blocking and to require all voice service providers to make all reasonable efforts to ensure that critical calls complete.

23. *Reasonable Analytics.* The *Report and Order* provides a safe harbor from liability under the Communication Act and the Commission's rules for voice service providers that block calls based on reasonable analytics that must include Caller ID authentication information, so long as consumers are given a meaningful opportunity to opt out. This safe harbor builds on the blocking the Commission made clear was permitted under the *Declaratory Ruling and Further Notice* and adds the requirement that voice service provides incorporate Caller ID authentication information into their analytics programs.

24. *Bad Actor Providers.* Additionally, the *Report and Order* establishes a safe harbor for terminating voice service providers that block calls from upstream voice service providers that, when notified that it is carrying bad traffic by the Commission, fails to effectively mitigate such traffic or fails to implement effective measures to prevent new and renewing customers from using its network to originate illegal calls. This safe harbor incentivizes bad-actor providers to better police their networks by raising the cost of passing bad traffic.

25. *Other Issues.* The *Report and Order* clarifies that any terminating voice service provider that blocks calls must designate a single point of contact for callers to report blocking errors at no charge. It further makes clear that blocking providers must investigate and resolve these blocking disputes in a reasonable amount of time that is consistent with industry best practices. To avoid abuse, the *Report and Order* declines to mandate a Critical Calls List at this time. It does, however, make clear that the Commission expects all voice service providers will take all possible steps to ensure that calls from PSAPs and government outbound emergency numbers are not blocked. Finally, it makes clear that calls to 911 should never be blocked unless the voice service provider knows without a doubt that the calls are unlawful.

Summary of Significant Issues Raised by Public Comments in Response to the IRFA

26. In the *Declaratory Ruling and Further Notice,* the Commission solicited comments on how to minimize the economic impact of the new rules

on small business. The Commission received four comments either directly referencing the IRFA or addressing small business concerns. Two of these comments focused on concerns about the ability of small businesses to implement STIR/SHAKEN and how this would impact the safe harbors proposed in the *Further Notice.* The remaining two comments focused on small business challenge mechanism issues.

27. *SHAKEN/STIR.* Both ITTA and Spoofcard raised concerns about safe harbors contingent on SHAKEN/STIR, noting that many small voice service providers have TDM networks and therefore will not be able to implement SHAKEN/STIR quickly. ITTA instead argues for a safe harbor for blocking based on reasonable analytics, while Spoofcard simply argues against blocking based solely on SHAKEN/STIR. The Commission recognizes that some small voice service providers will not be able to implement SHAKEN/STIR quickly. The first safe harbor the Commission adopts in the *Report and Order* does not prevent these voice service providers from blocking pursuant to the *Declaratory Ruling.* Additionally, as other effective Caller ID authentication technologies are developed, they may also satisfy the requirements of the first safe harbor. Finally, neither safe harbor the Commission adopts permits blocking solely on SHAKEN/STIR.

28. *Challenge Mechanisms.* Capio highlighted the importance of a robust challenge mechanism for small businesses. Both Capio and CUNA called for this mechanism to be offered free of charge, with CUNA noting that this is particularly important for small businesses such as credit unions. In the *Report and Order,* the Commission requires terminating voice service providers to designate a single point of contact for resolving blocking disputes and make contact information clear and conspicuous on their public-facing websites. The Commission further requires terminating voice service providers to resolve disputes in a reasonable amount of time, noting that what is reasonable may vary on a case-by-case basis. Finally, the Commission requires that this be offered at no charge to callers.

Response to Comments by the Chief Counsel for Advocacy of the Small Business Administration

29. Pursuant to the Small Business Jobs Act of 2010, which amended the RFA, the Commission is required to respond to any comments filed by the Chief Counsel for Advocacy of the Small Business Administration (SBA), and to provide a detailed statement of any change made to the proposed rules as a result of those comments. The Chief Counsel did not file any comments in response to the proposed rules in this proceeding.

Description of Projected Reporting, Recordkeeping, and Other Compliance Requirements for Small Entities

30. The *Report and Order* makes clear that voice service providers may block calls in certain circumstances and provides safe harbors for that blocking. The *Report and Order* also adopts certain protections for lawful callers. These changes affect small and large companies equally and apply equally to all the classes of regulated entities identified above.

31. *Reporting and Recordkeeping Requirements.* The *Report and Order* establishes blocking safe harbors that will require terminating providers that choose to block to maintain certain records to ensure that their blocking is in compliance with the safe harbor. The specific records that a terminating provider would need to retain will depend on the particular safe harbor the terminating provider is relying on as well as their specific blocking program. Terminating providers that choose to block calls based on reasonable analytics including caller ID authentication information will need to maintain records on calls blocked, as well as opt-out decisions made by consumers. These records are necessary to ensure that opt-out requests are honored and to aid in resolving blocking disputes. Terminating providers that choose to block all calls from a bad-actor upstream provider will need to retain information relevant to that decision to ensure that all requirements were met prior to blocking and to help respond to blocking disputes. Originating, intermediate, and terminating providers will also need to communicate with other providers regarding traceback, illegal traffic, and measures to prevent new customers from originating illegal traffic.

Steps Taken To Minimize the Significant Economic Impact on Small Entities, and Significant Alternatives Considered

32. The RFA requires an agency to describe any significant alternatives that it has considered in reaching its 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) an exemption from coverage of the rule, or any part thereof, for small entities.

33. The Commission considered feedback from the *Declaratory Ruling and Further Notice* in crafting the final order. The Commission evaluated the comments with the goal of removing regulatory roadblocks and giving industry the flexibility to block calls while still protecting the interests of lawful callers. For example, the rules the Commission adopts are permissive rather than mandatory, allowing small businesses to determine whether, and what type of, blocking is the correct approach for their network. A terminating provider may choose to block based on reasonable analytics, including caller ID authentication information, and benefit from that safe harbor. Should a terminating provider do so, they have flexibility to design their own reasonable analytics program and make that program either opt out or opt in. Alternatively, or in addition to that blocking, a terminating provider may choose to block all calls from an originating or intermediate provider that fails to meet the criteria the Commission lays out in the bad-actor provider safe harbor. The Commission recognizes small business concerns regarding the difficulty of deploying SHAKEN/STIR. Small businesses that cannot rapidly deploy SHAKEN/STIR have alternative blocking options, such as those from the *Declaratory Ruling and Further Notice* to ensure that they are not left behind. The Commission further took the concerns of small business into consideration in establishing the requirements to make challenging erroneous blocking simpler and at no cost to the caller.

34. The Commission does not see a need to establish a special timetable for small entities to reach compliance with the modification to the rules. No small business has asked for a delay in implementing the rules. Small businesses may avoid compliance costs entirely by declining to block robocalls, or may delay implementation of call blocking indefinitely to allow for more time to come into compliance with the rules. Similarly, there are no design standards or performance standards to consider in this rulemaking.

The Commission will send a copy of the *Report and Order,* including this FRFA, in a report to be sent to Congress and the Government Accountability Office pursuant to the Congressional Review Act.

Ordering Clauses

35. Pursuant to sections 4(i), 201, 202, 227, 227b, 251(e), 303(r), and 403 of the Communications Act of 1934, as amended, 47 U.S.C. 154(i), 201, 202, 227, 227b, 251(e), 303(r), and 403, the *Report and Order* is adopted and that part 64 of the Commission's rules, 47 CFR 64.1200, is amended.

List of Subjects in 47 CFR Part 64

Communications common carriers, Reporting and recordkeeping requirements, Telecommunications, Telephone.

Federal Communications Commission.

Marlene Dortch,

Secretary, Office of the Secretary.

Final Rules

For the reasons discussed in the preamble, the Federal Communications Commission amends 47 part 64 as follows:

PART 64—MISCELLANEOUS RULES RELATING TO COMMON CARRIERS

■ 1. The authority citation for part 64 continues to read as follows:

Authority: 47 U.S.C. 154, 201, 202, 217, 218, 220, 222, 225, 226, 227, 227b, 228, 251(a), 251(e), 254(k), 262, 403(b)(2)(B), (c), 616, 620, 1401–1473, unless otherwise noted; Pub. L. 115–141, Div. P, sec. 503, 132 Stat. 348, 1091.

■ 2. Amend § 64.1200 by
■ a. Adding paragraph (f)(17);
■ b. Revising paragraph (k) introductory text, paragraphs (k)(3) and (4) and adding paragraphs (k)(5) through (8).

The additions and revisions read as follows:

§ 64.1200 Delivery restrictions.

* * * * *

(f) * * *

(17) The term *effectively mitigate* means identifying the source of the traffic and preventing that source from continuing to originate traffic of the same or similar nature.

* * * * *

(k) Voice service providers may block calls so that they do not reach a called party as follows:

* * * * *

(3) A terminating provider may block a voice call without liability under the Communications Act or the Commission's rules where:

(i) Calls are blocked based on the use of reasonable analytics designed to identify unwanted calls;

(ii) Those analytics include consideration of caller ID authentication information where available;

(iii) A consumer may opt out of blocking and is provided with sufficient information to make an informed decision;

(iv) All analytics are applied in a non-discriminatory, competitively neutral manner;

(v) Blocking services are provided with no additional line-item charge to consumers; and

(vi) The terminating provider provides, without charge to the caller, the redress requirements set forth in paragraph (k)(8) of this section.

(4) A provider may block voice calls or cease to accept traffic from an originating or intermediate provider without liability under the Communications Act or the Commission's rules where the originating or intermediate provider, when notified by the Commission, fails to effectively mitigate illegal traffic within 48 hours or fails to implement effective measures to prevent new and renewing customers from using its network to originate illegal calls. Prior to initiating blocking, the provider shall provide the Commission with notice and a brief summary of the basis for its determination that the originating or intermediate provider meets one or more of these two conditions for blocking.

(5) A provider may not block a voice call under paragraphs (k)(1) through (4) of this section if the call is an emergency call placed to 911.

(6) A provider may not block calls under paragraphs (k)(1) through (4) of this section unless that provider makes all reasonable efforts to ensure that calls from public safety answering points and government emergency numbers are not blocked.

(7) For purposes of this section, a provider may rely on Caller ID information to determine the purported originating number without regard to whether the call, in fact originated from that number.

(8) Any terminating provider blocking pursuant to this subsection must provide a single point of contact, readily available on the terminating provider's public-facing website, for handling call blocking error complaints and must resolve disputes within a reasonable time. When a caller makes a credible claim of erroneous blocking and the terminating provider determines that the calls should not have been blocked, the terminating provider must promptly cease blocking calls from that number unless circumstances change. The terminating provider may not impose any charge on callers for reporting, investigating, or resolving blocking error complaints.

[FR Doc. 2020–17268 Filed 9–11–20; 8:45 am]

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DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 648

[Docket No. 200420–0118]
[RTID 0648–XA453]

Fisheries of the Northeastern United States; Scup Fishery; Adjustment to the 2020 Winter II Quota

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Temporary rule; in-season adjustment.

SUMMARY: NMFS adjusts the 2020 Winter II commercial scup quota and per-trip Federal landing limit. This action is necessary to comply with Framework Adjustment 3 to the Summer Flounder, Scup, and Black Sea Bass Fishery Management Plan that established the rollover of unused commercial scup quota from the Winter I to Winter II period. This notice is intended to inform the public of this quota and trip limit change.

DATES: Effective October 1, 2020, through December 31, 2020.

FOR FURTHER INFORMATION CONTACT: Laura Hansen, Fishery Management Specialist, (978) 281–9225; or *Laura.Hansen@noaa.gov.*

SUPPLEMENTARY INFORMATION: NMFS published a final rule for Framework Adjustment 3 to the Summer Flounder, Scup, and Black Sea Bass Fishery Management Plan in the **Federal Register** on November 3, 2003 (68 FR 62250), implementing a process to roll over unused Winter I commercial scup quota (January 1 through April 30) to be added to the Winter II period quota (October 1 through December 31) (50 CFR 648.122(d)). The framework also allows adjustment of the commercial possession limit for the Winter II period dependent on the amount of quota rolled over from the Winter I period. The Winter II period start date was changed from November 1 to October 1 as a part of Framework Adjustment 12 (83 FR 17314; April 19, 2018).

For 2020, the initial Winter II quota is 3,543,336 pounds (lb) (1,607 metric tons (mt)). The best available landings information indicates that 4,850,963 lb (2,200 mt) remain of the 10,027,597 lb (4,548 mt) Winter I quota. Consistent with Framework 3, the full amount of unused 2020 Winter I quota is being transferred to Winter II, resulting in a revised 2020 Winter II quota of

8,394,299 lb (3,808 mt). Because the amount transferred is between 4.5 and 5.0 million lb (2,041 mt and 2,268 mt), the Federal per trip possession limit will increase from 12,000 lb (5.4 mt) to 24,000 lb (10.9 mt), as outlined in the final rule that established the possession limit and quota rollover procedures for this year, published on May 15, 2020 (85 FR 29345).

Classification

NMFS issues this action pursuant to section 305(d) of the Magnuson-Stevens Act. This action is required by 50 CFR 648.122(d), which was issued pursuant to section 304(b), and is exempted from review under Executive Order 12866.

Pursuant to 5 U.S.C. 553(b)(B), there is good cause to waive prior notice and an opportunity for public comment on this action, as notice and comment would be contrary to the public interest. This action transfers unused quota from the Winter I Period to the Winter II Period to make it accessible to the commercial scup fishery. If implementation of this inseason action is delayed to solicit prior public comment, the objective of the fishery management plan to achieve the optimum yield from the fishery could be compromised. Deteriorating weather conditions during the latter part of the fishing year may reduce fishing effort, and could also prevent the annual quota from being fully harvested. This would conflict with the agency's legal obligation under the Magnuson-Stevens Fishery Conservation and Management Act to achieve the optimum yield from a fishery on a continuing basis, resulting in a negative economic impact on vessels permitted to fish in this fishery. Moreover, the rollover process being applied here was the subject of notice and comment rulemaking, and the range of potential trip limit changes were outlined in the final 2018 scup specifications that were published December 22, 2017; which were developed through public notice and comment. Based on these considerations, there is good cause under 5 U.S.C. 553(d)(3) to waive the 30-day delayed effectiveness period for the reasons stated above.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: September 9, 2020.

Jennifer M. Wallace,

Acting Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–20202 Filed 9–11–20; 8:45 am]

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Proposed Rules

Federal Register

Vol. 85, No. 178

Monday, September 14, 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.

OFFICE OF PERSONNEL MANAGEMENT

5 CFR Part 316

RIN 3206–AN92

Temporary and Term Employment

AGENCY: Office of Personnel Management.

ACTION: Proposed rule.

SUMMARY: The Office of Personnel Management (OPM) is proposing rules that would allow agencies to make term appointments in Science, Technology, Engineering, Mathematics (STEM) occupations; positions needed to stand-up, operate, and close-out time-limited organizations which have a specific statutory appropriation; and time-limited projects which have been funded through specific appropriation; for up to 10 years. OPM is proposing this rule to provide agencies with greater flexibility to staff foreseeably long-term projects of a STEM nature when the need for the work is not permanent, and other time-limited work when authorized by specific funding by Congress. The intended effect of this change is to allow agencies the flexibility and discretion to hire individuals with knowledge, skills and abilities tailored to a specific project or Congressional funded work that may not be required on a permanent basis or transferable to other functions of the agency. This longer term appointment may also assist agencies in recruiting individuals with specialized STEM knowledge who prefer the opportunity to work on a project-by-project basis to build their resumes and maintain current skills.

DATES: OPM must receive comments on or before November 10, 2020.

ADDRESSES: You may submit comments, identified by docket number and/or Regulatory Information Number (RIN) and title, by any of the following methods:

• *Federal Rulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.

All submissions received must include the agency name and docket number or RIN for this document. The general policy for comments and other submissions from members of the public is to make these submissions available for public viewing at *http://www.regulations.gov* as they are received without change, including any personal identifiers or contact information.

FOR FURTHER INFORMATION CONTACT: Michelle Glynn at (202) 606–1571, by fax at (202) 606–3340, TDD at (202) 418–3134, or by email at *Michelle.Glynn@opm.gov*.

SUPPLEMENTARY INFORMATION: OPM is proposing to amend its rules pertaining to term employment to allow agencies to make term appointments in certain STEM occupations; positions needed to stand-up, operate, and close-out time-limited organizations which have a specific statutory appropriation; and time-limited projects which have been funded through specific appropriation; for up to 10 years. To do this, OPM is amending its regulations at 5 CFR part 316, subpart C, by adding a new paragraph to § 316.301 which authorizes agencies to hire individuals into STEM occupations and positions needed in support of other time-limited work when authorized by specific funding by Congress, for up to 10 years.

Under current regulations at 5 CFR part 316, subpart C, agencies have the discretion to make term appointments for a period of more than 1 year but not more than 4 years to any positions for which the need for an employee's services is not permanent. If an agency wishes to extend the term beyond four years or make an initial appointment of more than 4 years, it must obtain OPM's approval. 5 CFR 316.301. OPM recognizes, however, that the work performed by STEM positions, and positions needed in support of projects and organizations specifically funded by Congress, often lasts longer than 4 years. For example, it may be cyclical and often project based (*e.g.,* developing a research concept, initial research to prove feasibility, and testing/evaluation) and must continue until the goal or purpose of the work has been accomplished. Such work may include, but is not limited to, the need to collect data or conduct research (including medical research) regarding a certain trend or phenomenon, sometimes over time; perform STEM analysis of this data or research; and prepare reports of findings and recommendations, based on the data and analysis; or develop and implement new Information Technology (IT) projects or programs. In some instances, the work performed by these individuals may be affected by environmental factors or other external circumstances beyond the agency's control, which may result in the need for a lengthier appointment.

In addition, a study using Burning Glass [1] data suggests that the pace of technological change is driving a STEM skills gap, with new technological advancements continually demanding new skills of STEM workers and making some existing skills obsolete. (Deming, David J.; Noray, Kadeem L, STEM Careers and the Changing Skill Requirements of Work. The National Bureau of Economic Research, Revised June 2019.) The authors state, ''Using a near-universe of online job vacancy data collected between 2007 and 2017 by the employment analytics firm Burning Glass Technologies (BG), we show that job skill requirements change significantly over the course of a decade. We use the BG data to calculate a systematic measure of job skill change, and show that skill demands in STEM occupations have changed especially quickly. The faster rate of change in STEM is driven both by more rapid obsolescence of old skills and by faster adoption of new skills.'' Moreover, there is a 13 percent projected growth of STEM jobs in the United States between 2017 and 2027. (Feiman, Joseph, Can STEM Qualifications Hold The Key To The Future Of Cybersecurity? (Forbes September 11, 2019), citing Economy Modeling Specialists International 2017, *ecs.org/vital-signs-notes-and-sources/.* Given this high demand, agencies will need the flexibility and agility to attract and retain talent, for a significant period of time, with up-to-date knowledge and training in the STEM fields for time-limited projects. This regulation will allow agencies to hire new STEM personnel and grant their own extension of the term appointments, if initially hired for less than 10 years, to allow agencies the ability to shape their

[1] Employment analytics firm Burning Glass Technologies (BGT).

workforce with greater agility to meet current and emerging mission needs. Affording agencies the option to use longer term appointments in lieu of contracting will allow the agency to have STEM hires to be placed in managerial or supervisory positions throughout the life cycle of a time-limited project. In addition, this regulation may help agencies better compete for STEM talent because Federal term employment will offer individuals more job security and benefits (*e.g.,* health insurance, life insurance and participation in the Thrift Savings Plan (TSP) than would contract work to individuals interested in working on special projects in order to keep abreast of new technology and enhance their skills.

OPM is proposing use of this authority for any STEM occupation, regardless of occupational group. This includes a variety of professional and technical positions in numerous occupational groups (*e.g.,* Natural Resources Management and Biological Sciences; medical, hospital, dental, and public health, and information technology).

In addition, OPM is proposing to extend this flexibility to cover positions needed in support of time-limited organizations or projects which have been specifically funded by Congress (*i.e.,* the organization or project has been funded outside of, or in addition to, an agency's usual appropriation). Work of this nature oftentimes requires positions to be filled initially for an unknown period of time. This uncertainty may result in recruitment and retention challenges when agencies are endeavoring to implement and support expressed Congressional interest these organizations or projects.

Under current OPM regulation, the duration of a term appointment is limited to four years and agencies may not extend a term appointment beyond four years without OPM approval. OPM is proposing that an agency may appoint individuals in STEM positions, positions needed in support of projects and organizations specifically funded by Congress, for a term of more than 1 year up to a term of 10 years, and, if the initial appointment is less than 10 years, an agency may extend the appointment up to the 10-year limit in increments determined by the agency. The vacancy announcement used to fill these position must state that the agency has the option of extending the term appointment up to the 10-year limit. No appointment made under this section may last longer than 10 years from the date of the initial appointment. When using this authority, an agency must follow the procedures and requirements of 5 CFR part 316, subpart C, for purposes of selection, tenure, and trial periods.

OPM's current regulations provide that OPM may approve the extension of 4-year appointment if the extension is ''clearly justified'' and is consistent with applicable statutory provisions. 5 CFR 316.301(b). OPM believes that agencies that perform time-limited projects that require the specialized STEM skills, or which are in support of organizations or projects specifically funded by Congress, are in the best position to assess how long the project should continue, and should have the ability to act quickly when, in the agency's judgment, additional time is necessary. OPM believes this flexibility promotes retention and continuity, workforce planning, and minimizes disruptions during project work because term employees may be less likely to leave if they know their employment for the anticipated life of the project is secure rather than face an uncertain future awaiting a process under which their agency requests and must receive OPM extension approval for continuing work on the same project. Accordingly, OPM is not requiring agencies to obtain OPM approval to take advantage of the full 10-year term appointment under the proposed rule. However, agencies will be subject to OPM oversight regarding whether they are using this appointment appropriately. OPM does not intend this rule to be a substitute for a permanent workforce or for appointing employees to permanent positions for work of a permanent nature. OPM intends this rule to be used only for STEM work that is genuinely time-limited in nature; or for positions needed to stand-up, operate, and close-out time-limited organizations which have a specific statutory appropriation; and time-limited projects which have been funded through specific appropriation.

Lastly, OPM is proposing to modify § 316.302(b)(7) to allow an agency to reappoint an individual who previously served on a 10-year term appointment to a position in the same agency appropriate for filling up to the 10-year maximum limit. Combined service under the previous term appointment(s) cannot exceed 10 years. We are also proposing to modify this section to include reappointments made pursuant to § 316.301(b), so as attune reappointments to such positions with those for 4-year term appointments made pursuant to § 316.301(a), and those made under proposed § 316.301(c). This proposed modification parallels current regulatory language for individuals serving on 4-year term appointments made under § 316.301(a).

OPM invites comments on all aspects of the proposed regulation. OPM is particularly interested in testing its conclusions regarding the anticipated benefits of this regulation, additional examples of relevant agency experience, information regarding any potential benefits of this rule or possible drawbacks, and suggestions for possible improvements.

Regulatory Flexibility Act

We certify that this regulation will not have a significant impact on a substantial number of small entities because it applies only to Federal agencies and employees.

E.O. 13563 and E.O. 12866, Regulatory Review

Executive Orders 13563 and 12866 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 rule has been designated a ''significant regulatory action,'' under Executive Order 12866.

Executive Order 13771: Reducing Regulation and Controlling Regulatory Costs

The Executive Order 13771 designation for any final rule resulting from these proposed regulations will be informed by comments received. The preliminary Executive Order 13771 designation for this proposed rule is deregulatory.

This regulation provides substantial flexibility to agencies, and therefore generates cost savings for these agencies. As a result, we consider this rule to be a deregulatory action under Executive Order 13771.

E.O. 13132, Federalism

This regulation will not have substantial direct effects on the States, on the relationship between the National Government and the States, or on distribution of power and responsibilities among the various levels of government. Therefore, in accordance with Executive Order 13132, it is determined that this rule does not have sufficient federalism implications to warrant preparation of a Federalism Assessment.

E.O. 12988, Civil Justice Reform

This regulation meets the applicable standard set forth in section 3(a) and (b)(2) of Executive Order 12988.

Unfunded Mandates Reform Act of 1995

This rule will not result in the expenditure by State, local, or tribal governments of more than $100 million annually. Thus, no written assessment of unfunded mandates is required.

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

This regulatory action will not impose any additional reporting or recordkeeping requirements under the Paperwork Reduction Act.

List of Subjects in 5 CFR Part 316

Employment, Government employees.

Office of Personnel Management.

Alexys Stanley,

Regulatory Affairs Analyst.

Accordingly, we propose to amend 5 CFR part 316 as follows:

PART 316—TEMPORARY AND TERM EMPLOYMENT

■ 1. Revise the authority citation for part 316 to read as follows:

Authority: 5 U.S.C. 3301, 3302; E.O. 10577, 3 CFR, 1954–1958 Comp., p. 218; 5 CFR 2.2(c).

Subpart C—Term Employment

■ 2. Amend § 316.301 by adding paragraph (c) to read as follows:

§ 316.301 Purpose and duration.

* * * * *

(c) An agency may make a term appointment for a period of more than 1 year but not more than 10 years to any science, technology, engineering, mathematics (STEM) position when the need for an employee's services is not permanent; or for positions needed to stand-up, operate, and close-out time-limited organizations which have a specific statutory appropriation; or time-limited projects which have been funded through specific congressional appropriation. An agency may extend an appointment made for more than 1 year but fewer than 10 years up to the 10-year limit in increments determined by the agency. The vacancy announcement must state that the agency has the option of extending a term appointment under this section up to the 10-year limit. No appointment made under this section may last longer than 10 years from the date of the initial appointment.

■ 3. Amend § 316.302 by revising paragraph (b)(7) to read as follows:

§ 316.302 Selection of term employees.

* * * * *

(b) * * *

(7) Reappointment on the basis of having left a term appointment prior to serving the 4-year maximum amount of time allowed under the appointment per § 316.301(a), the maximum time allowed for an appointment authorized under this paragraph (b), or the 10-year maximum amount of time allowed under § 316.301(c). Reappointment must be to a position in the same agency for filling under the original term appointment and for which the individual qualifies. Combined service under the original term appointment and reappointment must not exceed the 4-year limit for positions pursuant to § 316.301(a), the maximum time allowed for an appointment authorized under § 316.301(b), or the 10-year limit under § 316.301(c), as appropriate; or

* * * * *

[FR Doc. 2020–20038 Filed 9–11–20; 8:45 am]

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DEPARTMENT OF AGRICULTURE

Food Safety and Inspection Service

9 CFR Parts 352, 354, and 412

[Docket No. FSIS–2019–0019]

RIN 0583–AD78

Prior Label Approval System: Expansion of Generic Label Approval

AGENCY: Food Safety and Inspection Service, USDA.

ACTION: Proposed rule.

SUMMARY: The Food Safety and Inspection Service (FSIS) is proposing to amend its inspection regulations to expand the circumstances under which FSIS will generically approve the labels of meat, poultry, and egg products. FSIS is also proposing to cease evaluating generically approved labels submitted to FSIS for review.

DATES: Submit comments on or before November 13, 2020.

ADDRESSES: FSIS invites interested persons to submit comments on this document. Comments may be submitted by one of the following methods:

• *Federal eRulemaking Portal:* This website provides commenters the ability to type short comments directly into the comment field on the web page or to attach a file for lengthier comments. Go to *http://www.regulations.gov.* Follow the on-line instructions at that site for submitting comments.

• *Mail, including CD–ROMs, etc.:* Send to Docket Clerk, U.S. Department of Agriculture, Food Safety and Inspection Service, 1400 Independence Avenue SW, Mailstop 3758, Room 6065, Washington, DC 20250–3700.

• *Hand or Courier-Delivered Submittals:* Deliver to 1400 Independence Avenue SW, Room 6065, Washington, DC 20250–3700.

Instructions: All items submitted by mail or electronic mail must include the Agency name and docket number FSIS–2019–0019. Comments received in response to this docket will be made available for public inspection and posted without change, including any personal information, to *http://www.regulations.gov.*

Docket: For access to background documents or comments received, call (202) 720–5627 to schedule a time to visit the FSIS Docket Room at 1400 Independence Avenue SW, Room 6065, Washington, DC 20250–3700.

FOR FURTHER INFORMATION CONTACT: Rachel Edelstein, Acting Assistant Administrator, Office of Policy and Program Development, by telephone at (202) 720–0399.

SUPPLEMENTARY INFORMATION:

Executive Summary

To prevent the introduction of adulterated or misbranded products into commerce, the Food Safety and Inspection Service (FSIS) implements a prior approval program for labels intended to be used on federally inspected meat, poultry, and egg products (9 CFR part 412). Without approved labels, these products may not be sold, offered for sale, or otherwise distributed in commerce.

Certain categories of labels or renderings of such labels (sketch labels) must be submitted to FSIS for review and approval before use. However, FSIS considers certain labels that comply with the Agency's labeling rules to be ''generically'' approved. Such labels are not submitted to FSIS, because they are deemed approved and may be applied to product in commerce.

Generic label approval has been in place in some form since 1983. FSIS has previously expanded the categories of labeling claims eligible for generic approval, most recently in 2013 (78 FR 66826, November 7, 2013). FSIS has also published a proposed rule that, if finalized as proposed, would permit generic approval for egg product labels (83 FR 6314, February 13, 2018). FSIS is now proposing to expand the categories of meat, poultry, and egg product labels that it will deem generically approved and thus not required to be submitted to FSIS. Specifically, under this proposal the following labels would no longer need to be submitted to FSIS for approval: (1) Labels on products for export that deviate from FSIS requirements; (2) labels that list ingredients in the ingredients statement as being certified ''organic'' (*e.g.,* organic garlic) under the Agricultural Marketing Service (AMS) National Organic Program; (3) labels that display geographic landmarks, such as a foreign country's flag, monument, or map; (4) labels that make ''negative'' claims identifying the absence of certain ingredients or types of ingredients (*e.g.,* statements such as ''No MSG Added,'' ''Preservative Free,'' ''No Milk,'' ''No Pork,'' or ''Made Without Soy''); and (5) labels of products that receive voluntary FSIS inspection (*e.g.,* exotic species under 9 CFR part 352). Finally, FSIS is proposing to cease evaluating labels submitted to FSIS that are eligible for generic approval.

These reforms would result in an estimated 33.8 percent reduction in label submissions (based on fiscal year 2019 data) and reduce Agency costs expended to evaluate the labels (see Table 1). There will not be any negative food safety impacts from this proposal, based on FSIS's experience evaluating these types of labels and the ability of inspection personnel to continue to verify labeling requirements in the field.

There is no cost burden for the industry or FSIS for the proposed rule. This is shown in Table 1 below, which summarizes the costs and benefits of the proposed rule. Industry would experience cost savings of $468,864, annualized at the 7 percent discount rate over 10 years, from the reduction in preparing and submitting certain labels for FSIS evaluation. FSIS would experience cost savings of $235,690, annualized at the 7 percent discount rate over 10 years, from the reduction in label evaluations.

TABLE 1—SUMMARY OF ANNUALIZED COSTS AND BENEFITS

	Costs	Cost savings	Net benefits
Industry	$0	$468,864	$468,864
Agency	0	235,690	235,690
Total	0	704,554	704,554

Note: Estimates are annualized using a 7 percent discount rate over 10 years.

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I. Background

The Federal Meat Inspection Act (FMIA) (21 U.S.C. 601 *et seq.*), Poultry Products Inspection Act (PPIA) (21 U.S.C. 451 *et seq.*), and Egg Products Inspection Act (EPIA) (21 U.S.C. 1031 *et seq.*) direct the Secretary of Agriculture to maintain inspection programs designed to ensure that meat, poultry, and egg products are safe, wholesome, not adulterated, and properly marked, labeled, and packaged. These laws prohibit the sale of products under any false or misleading name, marking, or labeling and require the Secretary to approve product marking and labeling (21 U.S.C. 457(c), 607(d), and 1036(b)). The Department's longstanding interpretation of these provisions is that they require the Secretary or his or her representative to approve all labels to be used on federally inspected and passed, domestic and imported, meat, poultry and egg products, before the products may be distributed in commerce.

To implement these provisions, FSIS uses a prior approval program for labels on federally inspected meat, poultry, and egg products (9 CFR part 412). Without approved labels, meat, poultry, and egg products may not be sold, offered for sale, or otherwise distributed in commerce.

A. Current Label Regulations

The meat, poultry, and egg products labeling regulations require that meat, poultry, and egg products are truthfully labeled, and that the labeling provides the necessary product information for consumers to make informed purchasing decisions.

There are up to eight features required on meat, poultry, and egg product labels. The required features include: (1) The standardized, common or usual, or descriptive name, of the product (9 CFR 317.2(e), 381.117, and 590.411(c)(1)); (2) an ingredients statement containing the common or usual name of each ingredient of the product listed in descending order of predominance (9 CFR 317.2(f), 381.118, and 590.411(c)(1)); (3) the name and place of business of the manufacturer, packer, or distributor (9 CFR 317.2(g), 381.122, and 590.411(c)(2)); (4) an accurate statement of the net quantity of contents (9 CFR 317.2(h), 381.121, and 590.411(c)(4)); (5) the inspection legend, including the number of the official establishment (9 CFR 312.2(b), 317.2(i), 381.96, 381.123, and 590.411(c)(5)); (6) a handling statement if the product is perishable, *e.g.,* ''Keep Frozen'' or ''Keep Refrigerated'' (9 CFR 317.2(k), 381.125(a), and 590.410(a)(1)–(2)); (7) nutrition labeling for applicable meat and poultry products (9 CFR part 317, subpart B; part 381, subpart Y; and 590.411(e)); [1] and (8) safe handling instructions if the meat or poultry component of the product is not ready-to-eat (9 CFR 317.2(l) and 381.125(b)). In addition, imported meat, poultry, and egg products must bear the country of origin under the product name (9 CFR 327.14(b)(1), 381.205(a), and 590.950(a)(2)).

These required features must appear on the immediate containers of domestic products (9 CFR part 317, subpart A, and part 381, subpart N) and imported products (9 CFR part 327 and part 381, subpart T; 590.411(c); and 590.950(a)). The meat inspection regulations define an ''immediate container'' as ''the receptacle or other covering in which any product is directly contained or wholly or partially enclosed'' (9 CFR 301.2). The EPIA and poultry products inspection regulations define an ''immediate container'' as ''any consumer package; or any other container in which poultry products,

[1] Nutrition labeling for egg products must comply with the provisions of 21 CFR part 101, promogulated under the Federal Food, Drug, and Cosmetic Act and the Fair Packaging and Labeling Act [9 CFR 590.411(e)].

not consumer packaged, are packed'' (21 U.S.C. 1033(d)(1) and 9 CFR 381.1(b)).

The principal display panel, information panel, or other surface of the product label must prominently display the mandatory features. The first six features described above, and the labeling of country of origin for imported products in accordance with 9 CFR 327.14 and 381.205, have been required by the meat and poultry inspection regulations for decades. FSIS published regulations that require the nutrition labeling of cooked or heat-treated multi-ingredient meat and poultry products and the display of safe handling instructions in 1993 and 1994, respectively. Given industry's familiarity with these requirements, FSIS typically finds establishments in compliance with its labeling regulations.

The regulations contain other provisions to ensure that no statement, word, picture, design, or device that is false or misleading in any particular, or that conveys any false impression, or that gives any false indication of origin, identity, or quality, appears in any marking or other labeling (9 CFR 317.8, 381.129, and 590.411(f)(1)). Pursuant to the authority contained in section 7(e) of the FMIA (21 U.S.C. 607(e)), section 8(d) of the PPIA (21 U.S.C. 457(d)), and section 7(b) of the EPIA (21 U.S.C. 1036(b)), the Administrator of FSIS may withhold the use of any marking or labeling that is false or misleading, within the meaning of the FMIA, PPIA, and EPIA and their implementing regulations.

B. Current Prior Label Approval System

Under the current regulations, FSIS evaluates sketches of some labels for approval, and approves others generically, *i.e.,* without submission to FSIS for sketch approval. A sketch label is a printer's proof or other version that clearly shows all required label features, size, location, and indication of final color (9 CFR 412.1(d)). To obtain sketch label approval, domestic meat and poultry establishments, egg product plants, and certified foreign establishments that are eligible to export product to the United States, or their representatives, are required to submit sketch labels to FSIS for evaluation, except when the label is generically approved by the Agency under 9 CFR 412.2.

These firms submit sketch labels accompanied by FSIS Form 7234–1 (11/16/2011), ''Application for Approval of Labels, Marking or Device,'' to the Agency for evaluation. In addition to the required label information, any special claims or statements that the establishment intends to make (*e.g.,* quality claims, animal production raising claims, product origin claims, or nutrient content claims) must be included on the label, along with documentation supporting the claim. The label application must contain the basic information about the establishment and the product, including:

1. Establishment number;
2. Product name;
3. Product formulation;
4. Processing procedures and handling information;
5. Firm name and address;
6. Total available labeling space of the container;
7. Size of the principal display panel; and
8. The Hazard Analysis and Critical Control Point category under which the establishment is producing the meat or poultry product.

FSIS's Labeling and Program Delivery Staff (LPDS), in the Office of Policy and Program Development (OPPD), verifies that sketch labels comply with the applicable requirements. Since July 1, 1996, a final version of a verified sketch label does not have to be submitted to the Agency for evaluation and approval (60 FR 67444, December 29, 1995).[2] All labels are subject to verification for compliance with Agency regulations by FSIS inspectors to ensure that they are accurate, truthful, and not misleading.

C. Generic Label Approval

FSIS allows certain meat, poultry, and egg product labels that bear all required labeling features and that comply with the Agency's labeling regulations to be generically approved (9 CFR 412.2(a)(1)). Generically approved labels do not need to be submitted to FSIS for sketch approval before they can be used on products in commerce. Generic label approval requires that all mandatory label features are prominent and conform to FSIS regulations. Although such labels are not submitted to FSIS for approval, they are deemed to be approved and, therefore, may be applied to product in accordance with the Agency's prior label approval system.

Generic label approval has been in place in some form since 1983. That year, FSIS promulgated regulations that granted limited label approval authority to Inspectors-In-Charge (IICs) at official establishments and provided generic approval to limited types of labels (*e.g.,* labels for raw, single ingredient meat and poultry products) (48 FR 11410, March 18, 1983). The rulemaking's intent was to reduce the number of labels and other materials submitted for FSIS evaluation and to ease the paperwork burden on official establishments.

Even with the changes made by the rule, the number of labels submitted to the Agency continued to grow. During fiscal year 1991, the Agency processed approximately 167,500 labels. Of these, FSIS approved approximately 87,500 final labels and 60,000 sketch labels. FSIS disapproved approximately 20,000 labels.

On December 29, 1995, FSIS published a final rule that outlined the types of labels and modifications to labels that were deemed to be approved without submission to FSIS, provided that the label displayed all mandatory label features in conformance with applicable Federal regulations (60 FR 67444). The following labeling was deemed generically approved in that final rule: Labels on products with a standard of identity specified in FSIS regulations or *Food Standards and Labeling Policy Book*[3] (''*Policy Book*''); labels for raw, single-ingredient products that do not bear special claims; labels for containers of meat and poultry products sold under contract specifications to the Federal Government; labels for shipping containers that contain fully labeled immediate containers; labels for products not intended for human food (*e.g.,* for the pharmaceutical industry) and for poultry heads and feet to be exported for processing as human food, provided specific regulatory requirements are met; meat and poultry inspection legends that comply with 9 CFR parts 312, 316, and 381, subpart M; labeling on inserts, tags, liners, posters, and like devices that are not misleading and do not reference products; labels for consumer test products not intended for sale; and labels that were previously sketch approved by FSIS and contain no modifications or only certain listed modifications.

The 1995 final rule also transferred responsibility for maintaining labeling records from IICs to official establishments in the United States and to foreign establishments certified as meeting U.S. requirements under foreign inspection systems. For labels that still required FSIS review, the final rule removed the requirement that firms submit final labels for FSIS approval; thus, today, firms must only submit

[2] On February 13, 2018 FSIS published the *Egg Products Inspection Regulations* proposed rule (83 FR 6314). If the rule is finalized as proposed, FSIS will also not require submission of final versions of sketch labels for egg products.

[3] Available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulatory-compliance/labeling/Labeling-Policies.*

sketch labels. In the preamble to the 1995 final rule, FSIS stated that it intended to expand generic labeling after it completed an assessment of the modified system (60 FR 67444, 67448).

As explained in the preamble to the 2011 rule, FSIS completed this assessment in 1998 (76 FR 75809, December 5, 2011). FSIS surveyed industry to measure the effects of the generic approval program and sampled 1,513 labels for compliance with Federal regulations and policies. FSIS concluded that the great majority of establishments effectively used generically approved labels and that the gradual implementation of generic label provisions under the 1995 final rule was effective.

In 2011, FSIS published a proposed rule to replace the extensive list of generically approved meat and poultry labeling with a simpler set of label categories required to be submitted for Agency approval. FSIS proposed to require submission of: Labels for temporary approval, labels for products produced under religious exemption, labels for export with labeling deviations, and labeling with special statements and claims (76 FR 75809). FSIS also proposed to combine the label approval regulations for meat and poultry products (9 CFR 317.4 and 381.132) into a new part, 9 CFR part 412.

FSIS finalized the 2011 proposed rule on November 7, 2013 (78 FR 66826). The final rule codified the labeling categories and combined the meat and poultry labeling regulations as proposed. However, upon consideration of comments, FSIS finalized the rule with four changes (78 FR 66826, 66827). First, FSIS decided to continue to review generic labels that establishments voluntarily submit for approval; but, the Agency also made clear that such labels would receive lower review priority than non-generic labels. Second, FSIS clarified that special statements or claims (except for ''natural'' and negative claims) that are defined in FSIS's regulations or in the *Policy Book* are deemed to be generically approved. Third, FSIS determined that a label bearing a child-nutrition (CN) box will not be considered to have a special statement or claim on it that would require sketch approval by FSIS because such information was evaluated for approval by AMS. Finally, the Agency stated that it would no longer add new entries to the *Policy Book;* however, already existing entries may be revised or removed.

In the regulatory text of the 2013 final rule, FSIS stated that it would assess compliance by selecting samples of generically approved labels from establishments [9 CFR 412.2(a)(2)]. Additionally, after the final rule was published, FSIS received questions about the effectiveness of generic approval. To address these concerns and to establish a protocol for the future national assessment, the FSIS Office of Policy and Program Development (OPPD) conducted a limited assessment of labels.

OPPD conducted this assessment over a three-week period in September 2016.[4] Labeling policy experts traveled to five Federal meat and poultry establishments within the commuting area of FSIS headquarters in Washington, DC. Both large and small establishments were visited, including at least one corporation. In each establishment, the labeling policy experts assessed compliance of a representative sample of the generically approved label records on file. At the close of each assessment, the labeling policy experts held a closeout meeting with the FSIS inspection personnel and the establishment management. At this meeting, the labeling policy experts explained any deficiencies, determined if temporary approval was needed for deficient labels, and made recommendations for changes in the establishment's generic label approval and records management process. An assessment summary letter of this closeout meeting was provided to the establishment, inspection personnel, and the FSIS Office of Field Operations District Manager.

This assessment found a high level of compliance with the requirements. During examination of 270 labels, FSIS identified only three labels with deficiencies necessitating label revocation, and none of these deficiencies involved food safety. During the closing meetings with establishments, inspection and industry personnel determined that more outreach would significantly improve compliance. FSIS has initiated more outreach regarding labeling requirements, as discussed later in this document.

On February 13, 2018, FSIS published the proposed rule, *Egg Products Inspection Regulations* (83 FR 6314). This rule proposed several changes to FSIS's egg product inspection program, one of which adopted by reference FSIS's generic label approval regulation into the egg products regulations (9 CFR 590.412). If the rule is finalized as proposed, egg products will be eligible for generic approval of product labels on the same basis as meat and poultry product labels.

II. Proposed Rule

Since the 2013 rulemaking that established the categories of labels requiring sketch approval, FSIS has gained significant, additional experience evaluating labels required to be submitted and approved. From that experience, the Agency has concluded that the current label regulations continue to require industry to submit for approval a significant number of labels that could successfully be generically approved. FSIS is therefore proposing changes to its regulations to reduce the number of labels submitted for evaluation by FSIS and to lessen the paperwork burden on official establishments. The reduction in staff time spent approving these labels would allow the Agency to better focus on other consumer protection and food safety activities, such as developing guidance materials, answering labeling policy questions, providing outreach to stakeholders, and ensuring inspection program personnel (IPP) effectively verify that establishments meet labeling requirements. All labels used at official establishments would still be subject to FSIS verification activities in the field. These activities are further described in the section III. ''Surveillance and Enforcement'' below.

First, FSIS is proposing to extend generic label approval to products only intended for export that deviate from domestic labeling requirements, by removing 9 CFR 412.1(c)(2). FSIS maintains an Export Library that lists requirements for exported products that foreign authorities have officially communicated to FSIS, including labeling requirements.[5] At times, foreign country labeling requirements conflict with domestic requirements. FSIS regulations (9 CFR 317.7 and 381.128) permit export product labels to deviate from FSIS's domestic labeling requirements in order to comply with foreign country requirements or to be marketed more easily in a foreign country.[6] FSIS IPP verify whether product for export meets requirements listed in the Export Library, including

[4] Methodology available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulatory-compliance/labeling/labeling-policies/assessment-generically-approved-label.*

[5] The Export Library is available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/international-affairs/exporting-products/export-library-requirements-by-country.*

[6] Although there is no specific equivalent regulation for egg products, FSIS follows the same policy because such products, intended exclusively for export, must comply with foreign countries' requirements and are therefore not considered misbranded.

labeling, when certifying products for export. Verification of foreign requirements is ultimately determined by each foreign country's competent authority.

Second, FSIS is proposing to revise the types of ''special statements and claims'' requiring label submission by providing for generic approval of three additional types of claims. FSIS has observed through its prior label approval system that errors, omissions, and misrepresentations are rare on these types of labels. The proposed changes are to be made by amending 9 CFR 412.1(e) and 412.2(b).

The following types of claims would be generically approved:

a. ''Organic'' claims that appear in a product label's ingredients statement, which designate an ingredient as certified ''organic'' under AMS's National Organic Program. The ingredients statement on these product labels designates specific ingredients as organic (*e.g.,* organic garlic). FSIS would no longer require the submission and evaluation of supporting documentation to verify that such ingredients are indeed certified as organic by an AMS-recognized third-party certifier. However, FSIS would continue to require that labels certifying a total product as organic to be submitted for FSIS evaluation.

b. ''Geographic landmarks'' displayed on a product label, such as a foreign country's flag, monument, or map. For example, the following claims displayed on a product label would no longer require sketch approval: A polish flag depicted on a Polish sausage product label, or an outline of the State of Nevada depicted on a product label for beef produced in Nevada.

c. ''Negative'' claims made on product labels that identify the absence of certain ingredients or types of ingredients. For example, statements such as ''No MSG Added,'' ''Preservative Free,'' ''No Milk,'' ''No Pork,'' or ''Made Without Soy,'' on product labels that do not list these ingredients in the ingredients statement would no longer have to be evaluated by FSIS before use. However, FSIS evaluation of labels that bear negative claims relating to the raising of the animal from which the product is derived (*e.g.,* ''no antibiotics administered'') or negative claims relating to the use of genetically modified ingredients would continue to be required.

Third, FSIS is proposing to permit generic approval of the labels of products that receive voluntary FSIS inspection. FSIS provides several types of voluntary inspection services under the authority of the Agricultural Marketing Act (AMA) (7 U.S.C. 1621 *et seq.*), including inspection for: Rabbits (9 CFR part 354), certain non-amenable species of livestock and poultry animals, such as elk, bison, and migratory water fowl (9 CFR part 352, subpart A, and 9 CFR part 362); and products containing meat or poultry but are not under FSIS jurisdiction, *e.g.,* closed-faced sandwiches (9 CFR 350(c)). At present, labels for some products produced under these voluntary inspection programs are not covered under the Agency's generic approval regulations at 9 CFR 412. FSIS is proposing to permit generic approval for them on the same basis as amenable meat, poultry, and egg products by amending the relevant program regulations where needed to include references to 9 CFR part 412.[7] For clarity, FSIS will also modify 9 CFR 352.1 to update the section heading and remove unnecessary language.

Finally, FSIS is proposing to cease evaluating generically approved labels submitted voluntarily to LPDS for review. In the 2013 rulemaking that expanded the categories of labels eligible for generic approval, commenters requested to be allowed to continue submitting generic labels for FSIS guidance, evaluation, and approval. FSIS agreed to continue evaluating generic labels that were submitted, giving such labels secondary priority after labels requiring evaluation. Since the 2013 final rule, producers have become more familiar with FSIS's generic labeling requirements, and FSIS has provided additional guidance to assist them in designing compliant labels. Therefore, FSIS's evaluation of otherwise generic labels no longer represents an efficient use of Agency resources.

Comprehensive labeling guidance, including the *FSIS Compliance Guideline for Label Approval,*[8] is available at FSIS's website.[9] Information available includes a PowerPoint presentation titled ''Labeling 101,'' [10] which is used by the Agency as a teaching tool at workshops on meat and poultry label requirements. FSIS also provides guidance on allergen labeling and nutrition labeling,[11] a Label Submission Checklist,[12] a glossary of meat and poultry labeling terms,[13] the *Policy Book,* and questions and answers on various topics, such as generic approval, and the labeling of ingredients.[14]

FSIS will continue to conduct outreach to assist label submitters with labeling compliance in the form of webinars, industry group meetings, training for inspectors, guidance documents published on the FSIS website, and archived public askFSIS questions. Additionally, FSIS provides significant resources to assist label submitters on labels that require FSIS approval prior to use. These include askFSIS, a web portal that allows industry, IPP, and other stakeholders to submit technical and policy-related questions directly to OPPD.[15] Establishments may also contact FSIS for assistance with labeling questions. FSIS offers resources to assist small and very small plants, including the Small Plant Help Desk, which may be contacted by phone or email and answers questions on FSIS requirements.[16]

In June 2020, the USDA Office of Inspector General (OIG) concluded an audit of FSIS product labeling oversight (OIG audit #24601–0002–23, ''Controls Over Meat, Poultry, and Egg Product Labels'').[17] In response to the audit recommendations concerning FSIS oversight of generic labeling, the Agency agreed that it would continue to enhance its outreach efforts to ensure establishments are aware of applicable mandatory labeling features for generic

[7] The regulations providing for voluntary inspection of non-FSIS-jurisdiction products that contain meat or poultry (9 CFR 350(c)) and products containing non-amenable species of poultry (9 CFR part 362) already adopt 9 CFR part 412 by reference. For this reason, FSIS does not need to make additional regulatory changes to these parts in order to permit generic approval of labels for products receiving these services.

[8] Available at: *https://www.fsis.usda.gov/wps/wcm/connect/bf170761-33e3-4a2d-8f86-940c2698e2c5/Label-Approval-Guide.pdf?MOD=AJPERES.*

[9] Available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulatory-compliance/labeling.*

[10] Available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulatory-compliance/labeling/labeling-policies/basics-of-labeling/basics-labeling.*

[11] Available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulatory-compliance/labeling/labeling-policies/nutrition-labeling-policies/nutrition-labeling.*

[12] Available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulatory-compliance/labeling/labeling-procedures/label-submission-checklist.*

[13] Available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/food-safety-education/get-answers/food-safety-fact-sheets/food-labeling/meat-and-poultry-labeling-terms/meat-and-poultry-labeling-terms.*

[14] Available at: *https://www.fsis.usda.gov/wps/wcm/connect/bf170761-33e3-4a2d-8f86-940c2698e2c5/Label-Approval-Guide.pdf?MOD=AJPERES.*

[15] Available at: *https://askfsis.custhelp.com/.* See also, FSIS Directive 5620.1 Rev. 1, *Using askFSIS,* available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulations/directives.*

[16] The latest information on these resources is available at: *https://www.fsis.usda.gov/wps/portal/fsis/topics/regulatory-compliance/haccp/resources-and-information/svsp-brochure.*

[17] The audit report is available at: *https://www.usda.gov/oig/webdocs/24601-0002-23.pdf.*

labels. FSIS also agreed to update its internal policies to improve IPP label verification activities. Such verification activities are described in section III. ''Surveillance and Enforcement'' below. FSIS does not believe that the audit's findings or FSIS's responses to the audit affect this proposal.

III. Surveillance and Enforcement

Official establishments are required to label meat, poultry, and egg products with labels that are neither false nor misleading and that comply with FSIS's regulations. This is true whether the labels require sketch approval or may be generically approved. Establishments are required to keep records of all labels in accordance with 9 CFR 320.1(b)(10) for meat products, 9 CFR 381.175(b)(6) for poultry products, and 9 CFR 590.200(c) for egg products. These records must include a copy of the final label, the product formulation, processing procedures, and any supporting documentation needed to show that the label complies with the Federal meat, poultry, and egg regulations. Such records must be made available to any duly authorized representative of the Secretary upon request (9 CFR 320.4 and 590.200(b)).

IPP periodically perform a General Labeling Task assigned through FSIS's Public Health Inspection System (PHIS) as part of their regular label verification activities. This task is described in FSIS Directive 7221.1, *Prior Labeling Approval.* It includes verifying that establishments maintain records of the selected labels in accordance with 9 CFR 320.1(b)(10), 381.175(b)(6), and 590.200(c). IPP also verify that final labels applied to product contain all mandatory labeling features and are otherwise in compliance with the applicable regulations by evaluating establishments' labeling records and the labels themselves (*e.g.,* to verify that the ingredients statement on the label matches the product formula).

IPP document in PHIS any noncompliance found, *e.g.,* if a required labeling feature is missing or if a label requires LPDS evaluation but such evaluation is not documented in the records.[18] Establishments may take corrective action by obtaining label approval through LPDS, bringing the labels into compliance with a pressure sensitive sticker, or by replacing the noncompliant labels with labels that have received prior approval and are in compliance with FSIS's regulations. Final labels that are not in compliance with the regulations may still be granted temporary approval under the conditions listed in 9 CFR 412.1(f). IPP will retain any product bearing a label not in compliance with regulatory requirements as well as those that require, but have not received, LPDS approval. Pursuant to 9 CFR 500.8, FSIS may rescind approval of any false or misleading labels.[19]

FSIS relies on these verification tasks, in addition to evaluation by LPDS, to ensure that meat, poultry, and egg product labels are truthful and not misleading. Designating some product labels as generically approved, while maintaining inspection activities for all labels, promotes the effective use of Agency resources. This expansion of generic label approval will not affect consumer protection because FSIS will continue to evaluate labeling that has consumer safety or economic implications, *e.g.,* special statements and claims and requests for temporary approval. For example, FSIS will continue to review labeling that claims product is organic or all natural, makes statements regarding the raising of the animals from which products were derived, displays nutrition factual statements (*e.g.,* 10 g protein per serving) on the label, or includes certified claims (*e.g.,* ''Certified Gluten Free'') on the label.[20]

FSIS invites public comment on these proposed changes and requests data and additional suggestions for ways to make FSIS's generic labeling program more effective and efficient. FSIS considered three alternatives to this proposal: Taking no action; the proposed rule, except industry would still have the option to have LPDS evaluate labels that would otherwise be generically approved; and allowing all labels to be generically approved. Although FSIS ultimately decided on the current proposal, the Agency will continue to consider the alternatives described below (under the section titled ''Alternative Regulatory Approaches'') based on the information received.

IV. Executive Orders 12866 and 13563

Executive Orders (E.O.s) 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). E.O. 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. This proposed rule has been designated a ''significant'' regulatory action under section 3(f) of E.O. 12866. Accordingly, the rule has been reviewed by the Office of Management and Budget under E.O. 12866.

Need for the Rule

The proposed rule would expand the types of meat, poultry and egg product labels that can be generically approved by FSIS. This would reduce the number of labels evaluated by FSIS and reduce the costs to industry. The labels submitted for FSIS evaluation are becoming more complex and more time-consuming for industry to prepare and for FSIS to evaluate. The proposed rule would improve the efficiency of the label approval system by expanding generic labeling and making the system more convenient and cost efficient for the industry. This proposed rule also would enhance market efficiency by promoting a faster introduction of new products into the marketplace to meet consumer demand.

Baseline

Based on FSIS's Label Submission and Approval System (LSAS)[21] data, FSIS evaluated 15,459 unique labels during the 2019 fiscal year (FY). Of these, 5,229 (33.8 percent) would have been generically approved under the proposed rule. This amount (5,229) includes 632 labels currently eligible for generic approval, which firms voluntarily submitted for FSIS review. Many of the 15,459 labels were evaluated by FSIS more than once because they were returned to the producer to primarily make other types of corrections and then resubmitted for FSIS evaluation. FSIS has observed through its prior label approval system that corrections on the types of claims FSIS is proposing to generically approve are rare. In FY 2019, there were 26,158

[18] If IPP are not performing the General Labeling task but observe a product label that is not in compliance with Federal meat and poultry regulations, they will initiate a directed General Labeling task, retain affected product, and document the noncompliance in PHIS as described above.

[19] If FSIS rescinds or refuses to approve a label, it must explain its reasoning in a written notice, provide an opportunity for the establishment to modify the label, and advise the establishment of its appeal rights (9 CFR 500.8(b)).

[20] For an extensive list of labeling that requires FSIS approval, see the *FSIS Compliance Guideline for Label Approval.* Available at: *https://www.fsis.usda.gov/wps/wcm/connect/bf170761-33e3-4a2d-8f86-940c2698e2c5/Label-Approval-Guide.pdf?MOD=AJPERES.*

[21] FSIS's Label Submission and Approval System (LSAS) is a web-based software application that integrates and implements an electronic label application process for establishments to submit label applications to FSIS.

label adjudications, which included each time a label was evaluated. See Table 2 below for additional details.

each time a label was evaluated. See Table 2 below for additional details.

TABLE 2—LABEL EVALUATIONS AND ADJUDICATIONS, FY 2016–2019

[Pre proposed rule]

FSIS labels	2016	2017	2018	2019
Labels FSIS Would Not have Evaluated Under the Proposed Rule	8,534	5,812	6,025	5,229
Total Labels FSIS Evaluated *	22,846	17,958	17,635	15,459
Total Label Adjudications **	30,857	25,125	27,580	26,158

* This is the total number of labels FSIS evaluated, including the labels that would have been generically approved under the proposed rule.
** Label adjudications include some labels being revaluated.

FSIS expanded the types of labels and label changes that may be generically approved several times, starting in 1983 when the Agency evaluated 130,000 labels. In 1991, the number of labels evaluated peaked at 167,500. The 1995 final rule (60 FR 67444) amended the prior label approval process by expanding the types of labels and label changes that may be generically approved. From 2003–2010, the number of label adjudication per year averaged 57,457, with a minimum of 43,255 in 2003 and a maximum of 66,061 in 2010. The 2013 final rule (78 FR 66826, November 7, 2013) further expanded generic labeling, decreasing the number of label adjudications to 30,857 in FY 2016 (Table 2). FSIS also proposed to permit generic approval for certain egg product labels in 2018 (83 FR 6314, February, 13, 2018).

The number of FSIS label adjudications decreased after the expansions of generically approved labels. However, the remaining label submissions after each expansion are more time-consuming for industry to prepare and for FSIS to evaluate. This is because the labels requiring submission after each expansion are generally more complex, with special statements or claims that require FSIS to evaluate a significant amount of supporting documentation.

Expected Costs of the Proposed Rule

The proposed rule would not impose any new cost on producers that submit labels for FSIS evaluation. Instead, the proposed rule would reduce the regulatory burden on producers that currently submit labels for evaluation and does not change the recordkeeping requirements. Producers already are using generically approved labels and maintaining all labeling records, and thus are experienced in submitting labels for FSIS evaluation.

Expected Benefits of the Proposed Rule Industry Impacts

Industry would realize cost savings from the reduction in FSIS label submissions under the proposed rule. Industry is required to use FSIS Form 7234–1 (OMB control number: 0583–0092) for the initial FSIS label submission. The estimated time to complete this form is 75 minutes per response, which includes reviewing instructions, searching existing data sources, gathering and maintaining the data needed (recordkeeping), and completing and reviewing the collection of information.[22] FSIS estimates 15 minutes of the 75 minutes are dedicated to recordkeeping. The recordkeeping time is not included in the proposed rule's regulatory impact analysis because the recordkeeping requirements are not changing under the proposed rule; that is, even if the establishment does not need to submit the label to FSIS, the establishment is still required to maintain records to support the label. Therefore, the average industry time to prepare one label submission for FSIS evaluation is 60 minutes (75 minutes − 15 minutes). FSIS also assumed food scientists and technologists would perform this work at a mean hourly wage of $36.63.[23] A benefits and overhead factor of two[24] was applied to estimate the total labor cost per label submission of $73.26.

To determine the annual reduction of label submissions, FSIS relied on the average number of labels that FSIS would not have evaluated under the proposed rule from 2016 to 2019, which was 6,400 labels, ((8,534 + 5,812 + 6,025 + 5,229)/4), Table 2. Accordingly, FSIS estimates a decrease of 64,000 label evaluations over 10 years under the proposed rule (6,400 * 10). As shown in Table 3, FSIS estimates that industry would realize a discounted cost savings of $3,293,105 (at a 7 percent discount rate) and $3,999,505 (at a 3 percent discount rate) by FSIS generically approving an additional 64,000 labels over a 10-year period. The cost savings would be $468,864 when annualized at the 7 and 3 percent discount rate, over 10 years.

TABLE 3—ESTIMATED INDUSTRY COST SAVINGS

[2019 Dollars]

Total industry cost savings from reduced need for FSIS label evaluation	Present value cost savings at 7%	Present value cost savings at 3%
Total over 10 years	$3,293,105	$3,999,505
Annualized total over 10 years	468,864	468,864

[22] FSIS Form 7234–1 Application for Approval of Labels, Marking or Device. Last modified 11/16/2011. Available at: *https://www.fsis.usda.gov/wps/portal/fsis/forms/*.

[23] BLS Occupational Employment Statistics, Occupational Employment and Wages, May 2019. 19–1021 Food Scientists and Technologists. <*https://www.bls.gov/news.release/pdf/ocwage.pdfoes/current/oes191012.htm#nat*> Accessed on 4/30/2020. Last Modified 03/30/2020.

[24] To be consistent with analyses done by the Department of Health and Human Services, this analysis accounts for fringe benefits and overhead by multiplying wages by a factor of 2.

Agency Impacts

During FY 2019, FSIS employed 14 labeling analysts in LPDS with an average hourly salary of $64.75 (($47.52 * 36.25%) + 47.52 = $64.75 for a GS–13 step 1,[25] with an adjusted benefits factor of 36.25 percent).[26] On average, LPDS analysts evaluate labels four hours per day, five days a week, at a cost of $18,130 per week. If the proposed rule is adopted, LPDS analysts would evaluate labels for three hours per day, five days a week, at a cost of $13,598 per week, because of the reduction in labels submitted to FSIS.

If this proposed rule is adopted, the Agency would realize a discounted cost savings of $1,655,388 (at a 7 percent discount rate) and $2,010,484 (at a 3 percent discount rate) for adjudicating fewer labels over a 10-year period. The cost savings would be $235,690 when annualized at the 7 and 3 percent discount rate over 10 years. See Table 4 for additional details. However, this cost savings from fewer staff hours dedicated towards adjudicating labels would be redirected towards other Agency priority initiatives, such as developing and updating policy and guidance documents, answering questions from askFSIS and other sources, and performing outreach activities. We also anticipate an overall faster label review process from the decline in LPDS label evaluations. This would allow new labels to enter the market faster.

TABLE 4—ESTIMATED AGENCY COST SAVINGS

[2019 Dollars]

Total agency cost savings from reduced need for FSIS label evaluation	Present value cost savings at 7%	Present value cost savings at 3%
Total over 10 years	$1,655,388	$2,010,484
Annualized total over 10 years	235,690	235,690

Net Benefits

This proposed rule would be net beneficial because it would reduce the costs to establishments, from submitting fewer labels for FSIS evaluation, while imposing no additional cost burden. The net benefit derived from the proposed rule is estimated to be $4,948,493 ($3,293,105 in establishment savings plus $1,655,388 in Agency savings) discounted at the 7 percent discount rate over a 10-year period. When annualized at the 7 percent discount rate over 10 years, the net cost savings is estimated to be $704,554. See Table 5 for details.

TABLE 5—ESTIMATED AGENCY COST SAVINGS

[2019 Dollars]

Total agency and industry cost savings from reduced need for FSIS label evaluation	Present value cost savings at 7%	Present value cost savings at 3%
Total over 10 years	$4,948,493	$6,009,989
Annualized total over 10 years	704,554	704,554

Alternative Regulatory Approaches

The Agency considered three alternatives to the proposed rule. The proposed rule was chosen as the least burdensome regulatory approach. The summary of the costs and benefits for the considered alternatives are outlined in Table 6 below.

TABLE 6—REGULATORY ALTERNATIVES CONSIDERED

Alternative	Benefits	Costs	Net benefit
(1) Take No Action	No Benefit	No potential industry or Agency cost savings.	Net benefits are less than alternative 3.
(2) The Proposed Rule, Except Industry Would Still Have the Option to Have LPDS Evaluate Labels that Would Otherwise be Generically Approved.	Industry could benefit from additional FSIS evaluation.	Potential for inefficient use of Agency resources. Industry would also incur costs of submitting the labels and waiting for FSIS evaluation.	Net benefits are less than alternative 3. Although industry could marginally benefit from additional FSIS evaluation, sufficient guidance is available for labels that can be generically approved. Also, industry and the Agency would incur costs from submitting and evaluating such labels.

[25] Salary Table 2019–DCB for the locality pay area of Washington-Baltimore-Arlington, DC-MD-VA-WV-PA. Effective January 2019. Available at: *https://www.opm.gov/policy-data-oversight/pay-leave/salaries-wages/salary-tables/pdf/2019/DCB_h.pdf.*

[26] Nussle, Jim. (2008). M–08–13: MEMORANDUM FOR THE HEADS OF EXECUTIVE DEPARTMENTS AND AGENCIES. Executive Office of the President. Available at: *https://www.whitehouse.gov/sites/whitehouse.gov/files/omb/memoranda/2008/m08-13.pdf.*

TABLE 6—REGULATORY ALTERNATIVES CONSIDERED—Continued

Alternative	Benefits	Costs	Net benefit
(3) The Proposed Rule	Potential industry cost savings of $468,864 and Agency cost savings of $235,690, annualized at the 7 percent discount rate over 10 years.	No Cost	Net benefits are $704,554 annualized at the 7 percent discount rate over 10 years.
(4) Allow All FSIS Labels to be Generically Approved.	The Agency and industry would benefit from time savings by eliminating FSIS label evaluation.	Costs include potentially increasing the number of misbranded products.	Net benefits are less than alternative 3 as the potential costs of misbranded products from eliminating FSIS label evaluation outweighs the time savings benefit.

Alternative 1—No Action (Baseline)

FSIS considered keeping the current regulations and taking no action. Taking no action would mean that industry and the Agency would not experience costs savings from the reduction of labels submitted for FSIS evaluation under the proposed rule. Industry would therefore not realize the estimated reduction of 64,000 label submissions over 10 years and would not experience an annualized cost savings of $468,864 at the 7 percent discount rate over 10 years. The Agency would not experience time savings from the reduction of label evaluations. Therefore, the Agency rejects this alternative.

Alternative 2—The Proposed Rule, Except Industry Would Still Have the Option To Have LPDS Evaluate Labels That Would Otherwise be Generically Approved

FSIS considered an alternative of proposing the same generically approved label categories except FSIS would continue to evaluate those labels that would otherwise be generically approved. Currently, industry can submit labels that can be generically approved for voluntary FSIS evaluation, although this evaluation is not needed prior to entering the market. When industry submits these types of labels for voluntary FSIS evaluation, they are reviewed with a lower priority than other labels, and thus take more time for FSIS to approve. Although industry may marginally benefit from the additional FSIS evaluation, the process is inefficient and raises unnecessary costs. Industry could more quickly get FSIS assistance on these types of labels through other guidance, such as askFSIS.

In addition, FSIS would have to take the time to process and evaluate these labels, when reviewer time could be spent on higher priorities, such as food safety and policy related issues (*e.g.,* concerning allergens). Industry would also incur costs in preparing and submitting the labels for FSIS evaluation while they could get FSIS help through other outlets without incurring these expenses. For these reasons, FSIS rejects this alternative.

Alternative 3—The Proposed Rule

The proposed rule yields cost savings for both the industry and the Agency. There is no additional cost burden from the proposed rule. The potential cost savings for industry is $468,864, annualized at the 7 percent discount rate over 10 years. This covers the time industry saves from not preparing and submitting the labels for FSIS evaluation.

The potential cost savings for FSIS is $235,690, annualized at the 7 percent discount rate over 10 years. This covers the time FSIS saves from not evaluating the proposed generically approved labels. Since there is no additional burden for this proposed rule, FSIS determined this to be the preferred alternative.

Alternative 4—All Labels Are Generically Approved

FSIS also considered an alternative that would allow all labels to be generically approved, requiring no prior approval by FSIS. This alternative may increase the number of misbranded products going into commerce, as LPDS would no longer verify the information on complex labels. An increase in misbranded products that contain incorrect, false, or misleading information may result in a loss of consumer confidence in information on food labels. There is also cost associated with discarding and reprinting misbranded labels that the industry may suffer. Therefore, FSIS believes the labels that would still require prior evaluation under the proposed rule, such as labels with animal raising or natural claims, benefit from LPDS evaluation due to the complex nature and need for supporting documentation of these claims.

This alternative would yield time savings for industry from no longer preparing and submitting labels for FSIS evaluation. FSIS would also experience time savings from no longer evaluating these labels. However, the potential costs of misbranded products entering commerce, resulting from the elimination of all LPDS label evaluation, would outweigh the benefits of the time savings.

V. Regulatory Flexibility Act Assessment

The FSIS Administrator has made a preliminary determination that this proposed rule would not have a significant economic impact on a substantial number of small entities in the United States, as defined by the Regulatory Flexibility Act (5 U.S.C. 601). This determination was made because small producers would experience costs savings from the reduced number of label submissions for FSIS evaluation.

Based on LSAS and the Public Health Information System (PHIS) [27] data, FSIS estimates 92.3 percent (4,825/5,229) of the label submissions in 2019, which would have been generically approved under the proposed rule, are from small or very small Hazard Analysis and Critical Control Point (HACCP) sized establishments. Under the HACCP size definitions, large establishments have 500 or more employees and small establishments have fewer than 500 but more than 10 employees. Very small establishments have fewer than 10 employees or annual sales of less than $2.5 million. Small and very small establishments, like large establishments, follow the same standards for generic and sketch approval of labels. Small and very small producers, therefore, would not be disadvantaged because the proposed

[27] PHIS is FSIS's electronic data analytic system, used to collect, consolidate, and analyze data in order to improve public health.

rule would minimize the regulatory burden on all producers.

Based on 2019 LSAS data, about 12 percent (627/5,229) of labels that would have been generically approved under the proposed rule, were submitted from 19 label consultant firms. These firms are very small, usually having one to four employees. Many of these firms provide a range of services, including label courier services, label consultation and regulatory compliance, or label design. This proposed rule may impact their label courier business. However, the impact on these firms is small as their other business, such as label consultations, would not be affected. Therefore, this proposed rule would not have a significant economic impact on the small label consultant firms.

VI. Executive Order 13771

Consistent with E.O. 13771 (82 FR 9339, February 3, 2017), FSIS has estimated that this proposed rule would yield cost savings. Assuming a 7 percent discount rate, a perpetual time horizon, and a starting year of 2021, the proposed rule, if finalized, is estimated to yield approximately $502,337 (2016$) in annual cost savings. Therefore, if finalized as proposed, this rule would be an E.O. 13771 deregulatory action.

VII. Paperwork Reduction Act

FSIS has reviewed the paperwork and recordkeeping requirements in this proposed rule in accordance with the Paperwork Reduction Act (44 U.S.C. 3501, *et seq.*). The Administrator has determined that the proposed rule would not create any additional collection, paperwork, or recordkeeping burdens.

FSIS is proposing to expand the circumstances under which it will generically approve the labels of meat, poultry, and processed egg products. Under this final rule, more official and foreign establishments will be able to use the generic approval of product labels. As a result, fewer labels will need to be submitted and evaluated by FSIS. The relevant information collection, 0583–0092, Marking, Labeling, and Packaging, will have a net reduction of 6,400 burden hours because of the increased use of generic labeling.

VIII. E-Government Act

FSIS and USDA are committed to achieving the purposes of the E-Government Act (44 U.S.C. 3601, *et seq.*) by, among other things, promoting the use of the internet and other information technologies and providing increased opportunities for citizen access to Government information and services, and for other purposes.

IX. Executive Order 12988, Civil Justice Reform

This proposed rule has been reviewed under Executive Order 12988, Civil Justice Reform. Under this rule: (1) All State and local laws and regulations that are inconsistent with this rule will be preempted; (2) no retroactive effect will be given to this rule; and (3) no administrative proceedings will be required before parties may file suit in court challenging this rule.

X. Executive Order 13175, Consultation and Coordination With Indian Tribal Governments

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 and coordinate 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 on 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 does not to our knowledge, have tribal implications that require tribal consultation. If a tribe requests consultation, FSIS will work with the OTR to ensure meaningful consultation is provided where changes, additions, and modifications identified herein are not expressly mandated by Congress.

XI. USDA Non-Discrimination Statement

In accordance with Federal civil rights law and U.S. Department of Agriculture (USDA) civil rights regulations and policies, the USDA, its Agencies, offices, and employees, and institutions participating in or administering USDA programs are prohibited from discriminating based on race, color, national origin, religion, sex, gender identity (including gender expression), sexual orientation, disability, age, marital status, family/parental status, income derived from a public assistance program, political beliefs, or reprisal or retaliation for prior civil rights activity, in any program or activity conducted or funded by USDA (not all bases apply to all programs). Remedies and complaint filing deadlines vary by program or incident.

How To File a Complaint of Discrimination

To file a complaint of discrimination, complete the USDA Program Discrimination Complaint Form, which may be accessed online at *http://www.ocio.usda.gov/sites/default/files/docs/2012/Complain_combined_6_8_12.pdf,* or write a letter signed by you or your authorized representative.

Send your completed complaint form or letter to USDA by mail, fax, or email:

Mail: U.S. Department of Agriculture, Director, Office of Adjudication, 1400 Independence Avenue SW, Washington, DC 20250–9410.

Fax: (202) 690–7442.

Email: program.intake@usda.gov.

Persons with disabilities who require alternative means for communication (Braille, large print, audiotape, etc.), should contact USDA's TARGET Center at (202) 720–2600 (voice and TDD).

XIII. Environmental Impact

Each USDA agency is required to comply with 7 CFR part 1b of the Departmental regulations, which supplements the National Environmental Policy Act regulations published by the Council on Environmental Quality. Under these regulations, actions of certain USDA agencies and agency units are categorically excluded from the preparation of an Environmental Assessment (EA) or an Environmental Impact Statement (EIS) unless the agency head determines that an action may have a significant environmental effect (7 CFR 1b.4(b)). FSIS is among the agencies categorically excluded from the preparation of an EA or EIS (7 CFR 1b.4(b)(6)).

FSIS has determined that this proposed rule, which would refine the Agency's existing label approval program, will not create any extraordinary circumstances that would result in this normally excluded action having a significant individual or cumulative effect on the human environment. Therefore, this action is appropriately subject to the categorical exclusion from the preparation of an environmental assessment or environmental impact statement provided under 7 CFR 1b.4(6) of the U.S. Department of Agriculture regulations.

XIII. Congressional Review Act

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

XIV. Additional Public Notification

Public awareness of all segments of rulemaking and policy development is important. Consequently, FSIS will announce this **Federal Register** publication on-line through the FSIS web page located at: *http://www.fsis.usda.gov/federal-register.*

FSIS will also announce and provide a link to it through the FSIS *Constituent Update,* which is used to provide information regarding FSIS policies, procedures, regulations, **Federal Register** notices, FSIS public meetings, and other types of information that could affect or would be of interest to our constituents and stakeholders. The *Constituent Update* is available on the FSIS web page. Through the web page, FSIS is able to provide information to a much broader, more diverse audience. In addition, FSIS offers an email subscription service which provides automatic and customized access to selected food safety news and information. This service is available at: *http://www.fsis.usda.gov/subscribe.* Options range from recalls to export information, regulations, directives, and notices. Customers can add or delete subscriptions themselves and have the option to password protect their accounts.

List of Subjects

9 CFR Part 352

Food labeling, Meat inspection, Reporting and recordkeeping requirements.

9 CFR Part 354

Administrative practice and procedure, Animal diseases, Food labeling, Meat inspection, Rabbits and rabbit products, Reporting and recordkeeping requirements, Signs and symbols.

9 CFR Part 412

Food labeling, Food packaging, Meat and meat products, Meat inspection, Poultry and poultry products, Reporting and recordkeeping requirements.

For the reasons set forth in the preamble, FSIS is proposing to amend 9 CFR Chapter III as follows:

PART 352—EXOTIC ANIMALS AND HORSES; VOLUNTARY INSPECTION

■ 1. The authority citation for part 352 continues to read as follows:

Authority: 7 U.S.C. 1622, 1624; 7 CFR 2.17(g) and (i), 2.55.

■ 2. In § 352.7:

■ a. Revise the section heading;

■ b. Remove from the introductory text the phrase ''Wording and form of inspection mark.''; and

■ c. Add a sentence at the end of the introductory text.

The revision and addition read as follows:

§ 352.7 Marking and labeling of inspected products.

* * * * *

All labels intended for use on inspected and passed exotic animal products must be approved in accordance with Part 412 of this chapter.

* * * * *

PART 354—VOLUNTARY INSPECTION OF RABBITS AND EDIBLE PRODUCTS THEREOF

■ 3. The authority citation for part 354 continues to read as follows:

Authority: 7 U.S.C. 1622, 1624; 7 CFR 2.17(g) and (i), 2.55.

■ 4. Revise § 354.60 to read as follows:

§ 354.60 Approval of official identification.

All labels intended for use on inspected and passed rabbit products which bear any official identification must be approved in accordance with Part 412 of this chapter.

PART 412—LABEL APPROVAL

■ 5. The authority citation for part 412 continues to read as follows:

Authority: 21 U.S.C. 451–470, 601–695; 7 CFR 218, 2.53.

■ 6. In § 412.1, remove and reserve paragraph (c)(2) and revise paragraph (e) to read as follows:

§ 412.1 Label approval.

* * * * *

(e) ''Special statements and claims'' are statements, claims, logos, trademarks, and other symbols on labels as defined in this paragraph.

(1) The following are considered special statements and claims:

(i) Those not defined in the Federal meat and poultry products inspection regulations or the Food Standards and Labeling Policy Book;

(ii) ''Natural'' claims, regardless of whether they are defined in the Food Standards and Labeling Policy Book.

(iii) Health claims (including graphic representations of hearts), ingredient and processing method claims (*e.g.,* high-pressure processing), structure-function claims, claims regarding the raising of animals (*e.g.,* ''no antibiotics administered''), products labeled as organic (except for those where only individual ingredients are labeled as organic), and instructional or disclaimer statements concerning pathogens (*e.g.,* ''for cooking only'' or ''not tested for E. coli O157:H7'').

(2) The following are not considered special statements and claims:

(i) Allergen statements (*e.g.,* ''contains soy'') applied in accordance with the Food Allergen Labeling and Consumer Protection Act.

(ii) Negative claims regarding ingredients not listed in the ingredients statement (*i.e.,* ''No MSG Added,'' ''Preservative Free,'' ''No Milk,'' ''No Pork,'' or ''Made Without Soy'').

(iii) Statements that characterize a product's nutrient content in compliance with Title 9 of the CFR, such as ''low fat.''

(iv) Claims related to geographical significance, such as ''German Brand Made in the US,'' or those that make a country of origin statement on the label of any meat or poultry product ''covered commodity,'' or displays of geographic landmarks, such as a foreign country's flag, monument, or map.

* * * * *

■ 7. Revise § 412.2(b) to read as follows:

§ 412.2 Approval of generic labels.

* * * * *

(b) Generically approved labels are labels that bear all applicable mandatory labeling features (*i.e.,* product name, handling statement, ingredients statement, the name and place of business of the manufacturer, packer or distributor, net weight, legend, safe handling instructions, and nutrition labeling) in accordance with Federal regulations and do not bear special statements and claims as defined in paragraph 412.1(e) of this part.

Done at Washington, DC.

Paul Kiecker,

Administrator.

[FR Doc. 2020–17340 Filed 9–11–20; 8:45 am]

BILLING CODE 3410–DM–P

NUCLEAR REGULATORY COMMISSION

10 CFR Parts 50, 52, and 73

[NRC–2017–0227]

RIN 3150–AK19

Physical Security for Advanced Reactors

AGENCY: Nuclear Regulatory Commission.

ACTION: Preliminary proposed rule language; notice of availability.

SUMMARY: The U.S. Nuclear Regulatory Commission (NRC) is making preliminary proposed rule language for the Alternative Physical Security Requirements for Advanced Reactors rulemaking available to the public. The NRC is not requesting public comment at this time; however, the public will have an opportunity to provide comment when the proposed rule is published in the future.

DATES: The preliminary proposed rule language is available on September 14, 2020.

ADDRESSES: Please refer to Docket ID NRC–2017–0227 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–2017–0227. Address questions about NRC docket IDs to Carol Gallagher; telephone: 301–415–3463; email: *Carol.Gallagher@nrc.gov.* For technical questions, contact the individuals 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 preliminary proposed rule language is available in ADAMS under Accession No. ML20182A157.

• *Attention:* The Public Document Room (PDR), where you may examine and order copies of public documents is currently closed. You may submit your request to the PDR via email at *PDR.Resource@nrc.gov* or call 1–800–397–4209 between 8:00 a.m. and 4:00 p.m. (EST), Monday through Friday, except Federal holidays.

FOR FURTHER INFORMATION CONTACT: Dennis Andrukat, Office of Nuclear Material Safety and Safeguards, telephone: 301–415–3561, email: *Dennis.Andrukat@nrc.gov;* or Nanette Valliere, Office of Nuclear Reactor Regulation, telephone: 301–415–8462, email: *Nanette.Valliere@nrc.gov.* Both are staff of the U.S. Nuclear Regulatory Commission, Washington, DC 20555–0001.

SUPPLEMENTARY INFORMATION: The preliminary proposed rule language has been revised from the version provided in support of an April 22, 2020 public meeting. The revisions address NRC consideration of public comments received during and after the April 22, 2020, public meeting. The preliminary proposed rule language is available in ADAMS under Accession No. ML20182A157. For more information, see the public meeting summary at ADAMS Accession No. ML20189A274.

The NRC is not requesting public comment at this time; however, the public will have an opportunity to provide comment when the proposed rule is published in the **Federal Register** in the future.

Dated September 3, 2020.

For the Nuclear Regulatory Commission.

Ho K. Nieh,

Director, Office of Nuclear Reactor Regulation.

[FR Doc. 2020–19907 Filed 9–11–20; 8:45 am]

BILLING CODE 7590–01–P

FEDERAL COMMUNICATIONS COMMISSION

47 CFR Parts 1 and 2

[ET Docket No. 03–137, 13–84 and 19–226; Report No. 3155; FRS 16970]

Petitions for Reconsideration of Action in Proceedings

AGENCY: Federal Communications Commission.

ACTION: Petitions for Reconsideration.

SUMMARY: Petitions for Reconsideration (Petitions) have been filed in the Commission's proceeding by Donald J. Evans, on behalf of National Spectrum Manager's Association.

DATES: Oppositions to the Petitions must be filed on or before September 29, 2020. Replies to an opposition must be filed on or before October 9, 2020.

ADDRESSES: Federal Communications Commission, 445 12th Street SW, Washington, DC 20554.

FOR FURTHER INFORMATION CONTACT: Martin Doczkat, (202) 418–2435, Office of Engineering and Technology, Chief of Electromagnetic Compatibility Division, (202) 418–0636.

SUPPLEMENTARY INFORMATION: This is a summary of the Commission's document, Report No. 3155, released July 27, 2020. Petitions may be accessed online via the Commission's Electronic Comment Filing System at: *http://apps.fcc.gov/ecfs/.* The Commission will not send a Congressional Review Act (CRA) submission to Congress or the Government Accountability Office pursuant to the CRA, 5 U.S.C. 801(a)(1)(A), because no rules are being adopted by the Commission.

Subject: Proposed Changes in the Commission's Rules Regarding Human Exposure to Radiofrequency Electromagnetic Fields; Reassessment of Federal Communications Commission Radiofrequency Exposure Limits and Policies; Targeted Changes to the Commission's Rules Regarding Human Exposure to Radiofrequency Electromagnetic Fields, FCC 19–126, published 85 FR 18131, April 01, 2020 in ET Docket Nos. 03–137 (Terminated), 13–84 (Terminated), and 19–226. This document is being published pursuant to 47 CFR 1.429(e). *See also* 47 CFR 1.4(b)(1) and 1.429(f), (g).

Number of Petitions Filed: 1.

Federal Communications Commission.

Marlene Dortch,

Secretary, Office of the Secretary.

[FR Doc. 2020–16883 Filed 9–11–20; 8:45 am]

BILLING CODE 6712–01–P

DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 1, 7, 25, 44, and 52

[FAR Case 2018–002; Docket No. FAR Case 2018–0051, Sequence No. 1]

RIN 9000–AN62

Federal Acquisition Regulation: Protecting Life in Global Health Assistance

AGENCY: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Proposed rule.

SUMMARY: DoD, GSA, and NASA are proposing to amend the Federal Acquisition Regulation (FAR) to implement the Protecting Life in Global Health Assistance policy in connection with the Presidential Memorandum regarding ''The Mexico City Policy,'' dated January 23, 2017.

DATES: Interested parties should submit written comments at the address shown below on or before November 13, 2020 to be considered in the formation of the final rule.

ADDRESSES: Submit comments in response to FAR Case 2018–002 to *Regulations.gov: http://www.regulations.gov.* Submit comments via the Federal eRulemaking portal by searching for ''FAR Case 2018–002''. Select the link ''Comment Now'' that corresponds with ''FAR Case 2018–002''. Follow the instructions provided at the ''Comment Now'' screen. Please include your name, company name (if any), and ''FAR Case 2018–002'' on your attached document. If your comment cannot be submitted using *https://www.regulations.gov,* call or email the points of contact in the **FOR FURTHER INFORMATION CONTACT** section of this document for alternate instructions. Instructions: Please submit comments only and cite ''FAR case 2018–002'' in all correspondence related to this case. Comments received generally will be posted without change to *http://www.regulations.gov,* including any personal and/or business confidential information provided. To confirm receipt of your comment(s), please check *www.regulations.gov,* approximately two to three days after submission to verify posting.

FOR FURTHER INFORMATION CONTACT: *Farpolicy@gsa.gov* or call 202–969–4075. Please cite ''FAR Case 2018–002''.

SUPPLEMENTARY INFORMATION:

I. Background and Authority

A. Background

DoD, GSA, and NASA are proposing to revise the FAR to implement the Presidential Memorandum regarding ''The Mexico City Policy'', issued on January 23, 2017. This Presidential Memorandum reinstated the 2001 Presidential Memorandum on the ''Mexico City Policy,'' and directed the Secretary of State, in coordination with the Secretary of Health and Human Services, to implement a plan to extend the requirements of the Mexico City Policy to ''global health assistance furnished by all departments or agencies'' to the extent allowable by law.

The Mexico City Policy was first issued by President Reagan in 1984 and required foreign nongovernmental organizations (NGOs) to agree, as a condition of receiving U.S. Agency for International Development (USAID) family planning assistance, not to perform or actively promote abortion as a method of family planning with any source of funds. Under the Mexico City Policy, U.S. NGOs did not themselves have to agree that they would not perform or actively promote abortion as a method of family planning, but they were required to flow down the policy's requirements to foreign NGOs receiving family planning assistance under their awards. The Mexico City Policy was rescinded by President Clinton in 1993, reinstated by President Bush in 2001, and rescinded by President Obama in 2009. When in effect previously, the Mexico City Policy's requirements only applied to USAID family planning assistance and, from 2003–2009, to certain State Department activities; and it only applied to Federal assistance and not contracts.

To extend the Mexico City Policy as directed under the January 23, 2017, Presidential Memorandum, the Secretary of State approved on May 9, 2017, a plan to implement the manner in which U.S. Government Departments and Agencies will apply the provisions of the Mexico City Policy to foreign NGOs that receive U.S. funding for global health assistance. The plan, called ''Protecting Life in Global Health Assistance'' (PLGHA), expanded the application of the Mexico City Policy in three respects, to the extent allowable by law. First, it extended the policy to all affected Federal agencies. Second, it extended the policy to all global health assistance. Third, it required the extension of the policy to contracts in addition to Federal assistance. Each of these points is addressed further below. The PLGHA policy applies to foreign NGOs (including contractors); U.S. entities are not subject to the specific policy requirement not to perform or actively promote abortion as a method of family planning with any source of funds, but they must agree to flow down the policy requirements to foreign NGOs in accordance with the terms and conditions of their contracts.

1. Affected Federal Agencies

The PLGHA policy applies to all Federal agencies receiving global health assistance funding, including USAID, the State Department, the Department of Health and Human Services (HHS), and the DoD. To the extent other Federal agencies receive global health assistance funding through interagency transfer, they may also be required to apply the PLGHA terms in contracts with such funding, in accordance with FAR subparts 17.5 or 17.7.

2. Affected Global Health Assistance

The PLGHA policy applies to ''global health assistance''. This includes funding for international health programs, such as for Human Immunodeficiency Virus/Acquired Immunodeficiency Syndrome; maternal and child health; nutrition; infectious diseases, including malaria and tuberculosis; global health security; and voluntary family planning and reproductive health. More information about the scope of ''global health assistance'' is set forth below under ''II. Discussion and Analysis—Applicability of the PLGHA Policy.''

3. Affected Awards

The State Department's PLGHA implementation plan called for affected Federal agencies to take steps to apply the policy to Federal assistance (grants and cooperative agreements) and contracts. The PLGHA policy does not apply to global health assistance to foreign national or local governments, public international organizations and other multilateral entities in which sovereign nations participate.

For Federal assistance, affected Federal agencies developed a PLGHA standard provision, which they have included, starting in May 2017, in all new Federal assistance awards that use global health assistance funding and existing awards when amended to add new funding for global health assistance.

For contracts, this rule proposes to include a new clause entitled ''Protecting Life in Global Health Assistance'' in applicable contracts and subcontracts funded partially or wholly with global health assistance funding. The PLGHA implementation plan directs Federal agencies to take appropriate steps to apply the policy to new contracts; the plan would also apply to existing contracts, to the extent practicable, when modified to add funding.

4. Purpose

The PLGHA policy is consistent with the Presidential directive in the Presidential Memorandum—that no U.S. taxpayer money should support foreign organizations that perform or actively promote abortion as a method of family planning in other nations. Affected Federal agencies provide significant global health assistance funding through contracts each year. It is critical that such funding is also subject to the PLGHA terms and conditions to effect the President's directive.

All foreign contractors will be eligible to receive global health assistance funding if they agree to abide by the terms of the PLGHA policy in their contract or subcontract. PLGHA does not reduce the amount of global health assistance funding the United States Government makes available. The United States remains strongly committed to supporting health programs around the world.

5. More Information

More information about the 2017 Presidential Memorandum and the

PLGHA policy is available in the following:

• Presidential Memorandum on the Mexico City Policy (82 FR 8495, January 23, 2017).

• U.S. Agency for International Development's (USAID) website at *https://www.usaid.gov/global-health/legislative-policy-requirements.*

B. Authority

The President has broad discretion to set the terms and conditions on which the United States provides foreign assistance. The United States provides global health assistance through various Federal agencies, under the authorities granted to those Federal agencies, including the Foreign Assistance Act (FAA) (22 U.S.C. 2151 *et seq.*). The State Department and USAID, as well as other Federal agencies that receive foreign assistance funds from the State Department and USAID, rely on the authorities under the FAA. Under the FAA, the President is authorized to furnish foreign assistance for voluntary population planning, health programs, and to promote economic or political stability ''on such terms and conditions as [the President] may determine.'' See, *e.g.,* section 104(b) of the FAA (22 U.S.C. 2151b(b)) (assistance for family planning and population growth); section 104(c)(1) of the FAA (22 U.S.C. 2151b(c)(1)) (health assistance); section 531 of the FAA (22 U.S.C. 2346) (assistance to promote economic or political stability). The President, through the issuance of the January 23, 2017, Presidential Memorandum, has exercised his broad discretion to set the terms and conditions of U.S. foreign assistance relating to global health programs, including by applying the PLGHA policy to contracts.

II. Discussion and Analysis

A. Applicability of the PLGHA Policy

The PLGHA policy applies to all global health assistance funding, to the extent allowable by law. Under this policy, ''global health assistance funding'' is Federal funding used for international health activities that is authorized under the FAA, and funded from the Global Health Programs; Economic Support Fund; or Assistance for Europe, Eurasia, and Central Asia appropriations, including successor appropriations, under the annual Department of State, Foreign Operations, and Related Programs Appropriations Act.

Global health assistance funding excludes the following:

(1) Humanitarian assistance;

(2) USAID's American Schools and Hospitals Abroad Program activities;

(3) USAID's Food for Peace activities;

(4) USAID's Water Supply and Sanitation activities reported under Program Area HL.8 or successor program under the State Department's Foreign Assistance Standardized Program Structure; and

(5) USAID's Vulnerable Children activities reported under Program Area ES 4.1 or successor program under the State Department's Foreign Assistance Standardized Program Structure.

The policy applies to U.S. Government contracts funded with global health assistance funding that provide supplies or services for international health activities performed partially or wholly outside the United States (the 50 states, the District of Columbia, and outlying areas). This includes technical assistance and training of foreign individuals or entities as well as services listed in FAR 37.203(b)(1)–(6).

The policy will not apply to—

(1) Contracts at or below the micro-purchase threshold, as defined in FAR 2.101;

(2) Contracts for personal services with individuals; or

(3) Contracts for the acquisition of commercial items, including pharmaceuticals, medical supplies, logistics support, data management, freight forwarding, and warehousing.

B. Requirements Applicable to U.S. Contractors

As noted above, while U.S. contractors are not themselves subject to the PLGHA policy, they are required to flow down the PLGHA requirements to any foreign contractor with whom they subcontract, where applicable. Specifically, the proposed rule would require that, in signing a contract or subcontract funded with global health assistance funds, U.S. contractors and U.S. subcontractors at any tier agree that they shall not subcontract for global health assistance under the contract with a foreign contractor unless such foreign contractor agrees, as part of the subcontract, that it shall not, during the term of the award: (1) Perform or actively promote abortion as a method of family planning outside the United States (the 50 states, the District of Columbia, and outlying areas); or (2) provide financial support to any other foreign NGO that conducts such activities.

C. Requirements Applicable to Foreign Contractors

Foreign contractors that perform a contract with global health assistance funds will be subject to the PLGHA requirements. Specifically, such foreign contractors shall agree not to perform or actively promote abortion as a method of family planning or to provide financial support to any other foreign NGO that conducts such activities. In addition, a foreign contractor shall agree that it will not subcontract for global health assistance under its award with another foreign contractor unless such subcontractor agrees that it shall not, during the term of the award, (1) perform or actively promote abortion as a method of family planning outside the United States (the 50 states, the District of Columbia, and outlying areas) or (2) provide financial support to any other foreign NGO that conducts such activities. The term ''foreign NGO,'' as used in the rule, excludes public international organizations.

The contractor or subcontractor is not required to impose these requirements on foreign NGOs that are not receiving a subcontract and are only the beneficiaries of the training or technical assistance provided by the contractor or subcontractor.

D. Additional Requirements

The proposed rule further provides that, where the contract requires Government consent to subcontract, the contractor shall describe the due diligence it performed on the subcontractor related to the PLGHA requirements.

The proposed rule permits the furnishing of global health assistance funding under a contract to a foreign government or foreign-government-owned (parastatal) organization even if the organization includes abortion in its health program, provided that no global health assistance funds under the contract are used in support of the abortion activity of the foreign government or foreign-government-owned (parastatal) organization, and that such funds are placed in a segregated account to ensure they are not used for such activity.

Further, the proposed rule states that in the event of a conflict between the rule and an affirmative duty of a health care provider required under local law to provide abortion counseling or referrals, such compliance will not be considered a violation of the rule.

Finally, the proposed rule requires that the contractor insert certain terms of the clause in all subcontracts at any tier, except for subcontracts at or below the micro-purchase threshold; subcontracts for the acquisition of commercial items; and subcontracts for personal services with individuals.

E. Violations

The proposed rule sets forth specific requirements for responding to violations of contract terms. Specifically, the Government shall terminate the performance of work under the contract in accordance with the termination clause of the contract, if the foreign contractor violates its undertakings, unless the Government determines that other corrective action or remedy is warranted. If the contractor has reason to believe that the subcontractor has violated any requirement of the contract, the contractor shall consult with the contracting officer and provide full cooperation prior to terminating the subcontract or determining that other corrective action is warranted.

Furthermore, the proposed rule provides the circumstances under which violations by the subcontractor of any requirement in the contract will be imputed to the contractor—if the contractor knowingly subcontracts with a foreign subcontractor that does not abide by the requirements of the policy; where the contractor fails to make reasonable due diligence efforts prior to awarding a subcontract, and the subcontractor did not abide by its contractual terms required in the clause; or where the contractor knows, or has reason to know, of a violation by its subcontractor but fails to terminate the subcontract or take other corrective action.

III. Applicability to Contracts at or Below the Simplified Acquisition Threshold (SAT) and for Commercial Items, Including Commercially Available Off-the-Shelf (COTS) Items

A. Applicability to Contracts at or Below the SAT

The PLGHA policy does not apply to contracts below the micro-purchase threshold.

B. Applicability to Contracts for the Acquisition of Commercial Items, Including Commercially Available Off-the-Shelf Items

DoD, GSA, and NASA do not intend to apply the PLGHA policy to contracts for the acquisition of commercial items.

IV. Expected Cost Impact on the Public

The following is a summary of the impact on contractors awarded contracts that include the new FAR clause:

(1) All foreign contractors, whether prime or sub-recipients, of global health assistance funding must agree that (1) they will not perform or actively promote abortion as a method of family planning, or (2) provide financial support to any other foreign nongovernmental organization that conduct such activities. Notably, the new clause will be included in new awards and, to the extent practicable, in existing awards when modified to add funding. For the existing awards that will include the new clause, if a foreign prime contractor or subcontractor refuses to comply with this prohibition, the government and/or prime contractors would need to either not award a contract to that entity if they had otherwise been the selected offeror, or terminate an existing contract. The government or prime contractor would then have to find and contract or subcontract with an alternative entity that would agree to this prohibition. We expect that domestic entities would incur costs for ensuring the compliance of their foreign contractors with this rule.

(2) The primary costs to contractors (both U.S. and foreign) and foreign subcontractors associated with the rule may include increased compliance costs such as training, development of compliance tools, ongoing monitoring activities, etc.

(3) Foreign contractors and foreign subcontractors will be required to allow the Government, at any reasonable time announced or unannounced, to—

(i) Inspect the documents and materials maintained or prepared by the contractor in the usual course of its operations that describe the health activities implemented by the contractor or subcontractor, including reports, brochures and service statistics;

(ii) Observe the health activities conducted by the contractor or subcontractor;

(iii) Consult with health care personnel of the contractor or subcontractor; and

(iv) Obtain a copy of audited financial statements or reports of the contractor or subcontractor; as applicable.

(4) All contractors will be required to request Government approval prior to treating the health activities of two or more organizations that are affiliates as separate, when determining whether a foreign firm is eligible for a subcontract funded with global health assistance funding. This would entail contract employees preparing and submitting a written justification to the government explaining why the entities should be considered separate.

(5) When preparing requests for a contracting officer's consent to subcontract, contractor must include a written description of the due diligence it has performed on the subcontractor relating to the requirements of the new clause. Activities could include inspecting financial and programmatic documents; interviewing witnesses and employees; and inspecting facilities; as well as drafting the description.

(6) All contractors will be required to review the health activities of subcontractors that are suspected of violating the terms of the FAR clause 52.225–X and to provide the results of any of those reviews to the Government. This would require contractor employees to inspect financial and programmatic documents; interview witnesses and employees; and inspect facilities.

(7) All contractors will be required to place in a segregated account any global health assistance funds transferred to a foreign government or parastatal that includes abortion in its health program. This would require the contractor overseeing that the foreign government or parastatal contractor or subcontractor is maintaining a separate bank account. The foreign government or parastatal contractor or subcontractor would have to open and maintain a separate bank account for these award funds.

DoD, GSA, and NASA have performed a regulatory cost analysis on this proposed rule. The following is a summary of the estimated cost calculated in from FY2016–FY2018 at a 3 and 7 percent discount rate and in perpetuity:

Summary	Public	Government	Total
Present Value (3%) (millions)	$30.0	$39.3	$69.3
Annualized Costs (3%) (millions)	.9	1.2	2.1
Present Value (7%) (millions)	21.6	28.0	49.6
Annualized Costs (7%) (millions)	1.5	2.0	3.5

V. Executive Orders 12866 and 13563

Executive Orders (E.O.s) 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). E.O. 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. This is a significant regulatory action and, therefore, was subject to review under section 6(b) of E.O. 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

VI. Executive Order 13771

This proposed rule is considered an E.O. 13771 regulatory action. We estimate that this rule generates $2.1 million in annualized costs, discounted at 7 percent relative to year 2016, over a perpetual time horizon. More details on the costs associated with this rule can be found in the expected cost impact section of the rule.

VII. Regulatory Flexibility Act

DoD, GSA, and NASA do not expect this rule to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.* However, an Initial Regulatory Flexibility Analysis (IRFA) has been performed, and is summarized as follows:

This action is necessary to implement the Presidential Memorandum Regarding the Mexico City Policy, issued on January 23, 2017. This Presidential Memorandum reinstated the 2001 Presidential Memorandum on the ''Mexico City Policy,'' and directed the Secretary of State, in coordination with the Secretary of Health and Human Services, to implement a plan to extend the requirements of the Mexico City Policy to ''global health assistance furnished by all departments or agencies'' to the extent allowable by law.

To extend the Mexico City Policy as directed under the January 23, 2017, Presidential Memorandum, the Secretary of State approved, on May 9, 2017, a plan to implement the manner in which U.S. Government Departments and Agencies will apply the provisions of the Mexico City Policy to foreign NGOs that receive U.S. funding for global health assistance. The plan, called ''Protecting Life in Global Health Assistance'' (PLGHA), expanded the application of the Mexico City Policy in three respects, to the extent allowable by law. First, it extended the policy to all affected Federal agencies. Second, it extended the policy to all global health assistance. Third, it required the extension of the policy to contracts in addition to Federal assistance.

The objective of this proposed rule is to ensure contractors are aware of the requirement to comply with the PLGHA policy, pursuant to the PLGHA plan approved by the Secretary of State further to the January 23, 2017, Presidential memorandum.

The President has broad discretion to set the terms and conditions on which the United States provides foreign assistance. The United States provides global health assistance through various Federal agencies, under the authorities granted to those Federal agencies, including the Foreign Assistance Act (FAA) (22 U.S.C. 2151 *et seq.*). The Department of State and USAID, as well as other Federal agencies that receive foreign assistance funds from the Department of State and USAID, rely on the authorities under the FAA. Under the FAA, the President is authorized to furnish foreign assistance for voluntary population planning, health programs, and to promote economic or political stability ''on such terms and conditions as [the President] may determine.'' See, *e.g.,* section 104(b) of the FAA (22 U.S.C. 2151b(b)) (assistance for family planning and population growth); section 104(c)(1) of the FAA (22 U.S.C. 2151b(c)(1)) (health assistance); section 531 of the FAA (22 U.S.C. 2346) (assistance to promote economic or political stability). The President, through the issuance of the January 23, 2017, Presidential Memorandum, has exercised his broad discretion to set the terms and conditions of U.S. foreign assistance relating to global health programs, including by applying the PLGHA policy to contracts.

The PLGHA policy applies to foreign nongovernmental organizations (including contractors). Although U.S. entities are not themselves subject to the policy (not to perform or actively promote abortion as a method of family planning with any source of funds), they must agree to flow down the policy requirements to foreign nongovernmental organizations under their contracts.

This proposed rule is not expected to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Analysis Act, 5 U.S.C. 601, *et seq.* U.S. contractors are not themselves subject to the policy (not to perform or actively promote abortion as a method of family planning with any source of funds), but they must agree to flow down the PLGHA requirements to subcontractors and ensure that foreign subcontractors comply with the policy. This rule applies to foreign prime contractors.

Based on data available from FY2016–FY2018, we estimate that approximately 253 contractors would be affected by this rule. Of that we estimate that 45 small businesses would be affected; equating to 18 percent of the total contractors affected.

This rule does impose new reporting, recordkeeping and other compliance requirements. The rule includes requirements for access to documents, records, and processes to conduct inspections for compliance purposes. U.S. contractors will be responsible for the oversight of their foreign subcontractors. The foreign contractors will be subject to this requirement. Instances of these requirements are—

a. 52.225–XX(c)(2)(i) Inspection of documents and materials (foreign primes)—

''(c) *Foreign prime contractors.* This paragraph (c) applies only to foreign prime contractors, and does not affect any contractual rights between U.S. prime contractors and the U.S. Government:

(2) The Contractor shall allow authorized representatives of the Government to, at any reasonable time, announced or unannounced, consistent with the terms of this contract—

(i) Inspect the documents and materials maintained or prepared by the Contractor in the usual course of its operations that describe the health activities implemented by the Contractor, including reports, brochures, and service statistics'';

b. 52.225–XX(j)(1)(ii)(A) Inspection of documents and materials (foreign subcontractors)—

''(j) *Obligations regarding foreign subcontracts.*

(1) The Contractor shall ensure that foreign subcontractors at any tier that receive global health assistance funding agree to the following additional terms:

(ii) The Contractor and authorized representatives of the Government may, at any reasonable time, announced or unannounced, consistent with the terms of this contract, perform any of the following:

(A) Inspect the documents and materials maintained or prepared by the subcontractor in the usual course of its operations that describe the health activities of the subcontractor, including reports, brochures, and service statistics.''

c. 52.225–XX(e) Consent to subcontract (all primes and subcontractors)—

''(e) *Consent to subcontract.* If the contract includes the clause at FAR 52.244–2, Subcontracts, and requires the Contractor to obtain consent prior to entering into a subcontract, then the Contractor shall provide to the Contracting Officer, in the consent request, a description of the due diligence performed by the Contractor on the subcontractor relating to the requirements in this clause.

d. 52.225–XX(g)(2) Review of health program for violations (all primes and subcontractors)—

''(g) *Government independent inquiries.*

(2) In the event that the Contractor or the Government has reason to believe that a foreign subcontractor may have violated the requirements of this clause, the Contractor shall review the health program of the foreign subcontractor to determine whether such a violation has occurred. The Contractor shall provide the Contracting Officer the results of the review.''

e. 52.225–XX(j)(2) and (j)(3) Review of health program for violations (foreign subcontractors)—

''(j) *Obligations regarding foreign subcontracts.*

(2) In the event that the Contractor or the Government has reason to believe that a foreign subcontractor may have violated the

requirements of this clause, the Contractor shall review the health program of the subcontractor to determine whether such a violation has occurred.

(3) If the Contractor has reason to believe that the subcontractor has violated any requirement of this clause, the Contractor shall consult with the Contracting Officer and provide full cooperation prior to terminating the subcontract or determining that other corrective action is warranted.''

The rule does not duplicate, overlap, or conflict with any other Federal rules. DoD, GSA, and NASA were unable to identify any alternatives to the rule that would reduce the impact on small entities and still meet the requirements.

The Regulatory Secretariat Division has submitted a copy of the IRFA to the Chief Counsel for Advocacy of the Small Business Administration. A copy of the IRFA may be obtained from the Regulatory Secretariat Division. DoD, GSA, and NASA invite comments from small business concerns and other interested parties on the expected impact of this rule on small entities.

DoD, GSA, and NASA will also consider comments from small entities concerning the existing regulations in subparts affected by the rule in accordance with 5 U.S.C. 610. Interested parties must submit such comments separately and should cite 5 U.S.C. 610 (FAR Case 2018–002), in correspondence.

VIII. Paperwork Reduction Act

The Paperwork Reduction Act (44 U.S.C. chapter 35) applies. The proposed rule contains information collection requirements. Accordingly, the Regulatory Secretariat Division has submitted a request for approval of a new information collection requirement concerning FAR Case 2018–002, Protecting Life in Global Health Assistance to the Office of Management and Budget.

A. Public reporting burden for this collection of information is estimated to average 35.8 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.

The annual reporting burden is estimated as follows:

* *Respondents:* 253.
* *Responses per respondent:* 4.3.
* *Total annual responses:* 1,089.
* *Preparation hours per response:* 35.8.
* *Total response burden hours:* 38,992.

B. Request for Comments Regarding Paperwork Burden.

Submit comments, including suggestions for reducing this burden, not later than November 13, 2020 to: FAR Desk Officer, OMB, Room 10102, NEOB, Washington, DC 20503, and a copy to the General Services Administration, Regulatory Secretariat Division (MVCB), 1800 F Street NW, 2nd Floor, Washington, DC 20405–0001.

Public comments are particularly invited on: Whether this collection of information is necessary for the proper performance of functions of the FAR, and will have practical utility; whether our estimate of the public burden of this collection of information is accurate, and based on valid assumptions and methodology; ways to enhance the quality, utility, and clarity of the information to be collected; and ways in which we can minimize the burden of the collection of information on those who are to respond, through the use of appropriate technological collection techniques or other forms of information technology.

Requesters may obtain a copy of the supporting statement from the General Services Administration, Regulatory Secretariat Division (MVCB), 1800 F Street NW, 2nd Floor, Washington, DC 20405–0001. Please cite OMB Control Number 9000–00XX, Title, in all correspondence.

The rule contains information collection requirements that require the approval of the Office of Management and Budget under the Paperwork Reduction Act (44 U.S.C. chapter 35).

List of Subjects in 48 CFR Parts 1, 7, 25, 44, and 52

Government procurement.

William F. Clark,

Director, Office of Government-wide Acquisition Policy, Office of Acquisition Policy, Office of Government-wide Policy.

Therefore, DoD, GSA, and NASA propose amending 48 CFR parts 1, 7, 25, 44, and 52 as set forth below:

■ 1. The authority citation for 48 CFR parts 1, 7, 25, 44, and 52 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 51 U.S.C. 20113.

PART 1—FEDERAL ACQUISITION REGULATIONS SYSTEM

■ 2. In section 1.106, amend the table by adding an entry for ''52.225–XX'' in numerical order to read as follows:

1.106 OMB approval under the Paperwork Reduction Act.

* * * * *

FAR segment	OMB control No.
* * *	* *
52.225–XX	9000–XXXX
* * *	* *

PART 7—ACQUISITION PLANNING

■ 3. Add section 7.10X to read as follows:

7.10X Additional requirements for global health assistance acquisitions.

When planning to procure supplies or services for global health assistance, the requiring activity is responsible for notifying the contracting officer, in writing, when the contract will be funded partially or wholly with global health assistance funding, as defined in 25.100X–4.

PART 25—FOREIGN ACQUISITION

■ 4. Add section 25.100X to read as follows:

25.100X Protecting Life in Global Health Assistance.

25.100X–1 Scope of section.

This section implements the ''Protecting Life in Global Health Assistance'' policy approved by the Secretary of State on May 9, 2017, as directed by the Presidential Memorandum regarding The Mexico City Policy, dated January 23, 2017.

25.100X–2 Authority.

(a) Foreign Assistance Act of 1961 (22 U.S.C. 2151 *et seq.*).

(b) Presidential Memorandum on the Mexico City Policy (Memorandum of January 23, 2017, 3 CFR, 2017 Comp., p. 435.).

25.100X–3 Applicability.

This section applies to all executive agencies that implement programs or activities funded partially or wholly with global health assistance funding as defined in 25.100X–4.

25.100X–4 Definitions.

As used in this section—

Abortion as a method of family planning means abortion when it is for the purpose of spacing births. This includes, but is not limited to, abortions performed for the physical or mental health of the mother and abortions performed for fetal abnormalities, but does not include abortions performed if the life of the mother would be endangered if the fetus were carried to term, or abortions performed following rape or incest.

Actively promote abortion as a method of family planning means for an organization to commit resources, financial or other, in a substantial or continuing effort to increase the availability or use of abortion as a method of family planning.

(1) This includes, but is not limited to, the following activities:

(i) Operating a service-delivery site that provides, as part of its regular program, counseling, including advice and information, regarding the benefits and/or availability of abortion as a method of family planning;

(ii) Providing advice that abortion as a method of family planning is an available option or encouraging women to consider abortion (passively responding to a question regarding where a safe, legal abortion may be obtained is not considered active promotion if a woman who is already pregnant specifically asks the question, she clearly states that she has already decided to have a legal abortion, and the healthcare provider reasonably believes that the ethics of the medical profession in the host country requires a response regarding where it may be obtained safely and legally);

(iii) Lobbying a foreign government to legalize or make available abortion as a method of family planning or lobbying such a government to continue the legality of abortion as a method of family planning; and

(iv) Conducting a public information campaign outside the United States (the 50 states, the District of Columbia, and outlying areas), regarding the benefits and/or availability of abortion as a method of family planning.

(2) Excluded from this definition are referrals for abortion as a result of rape or incest, or if the life of the mother would be endangered if she were to carry the fetus to term. Also excluded from this definition is the treatment of injuries or illnesses caused by legal or illegal abortions, for example, post-abortion care.

(3) Action by an individual acting in the individual's capacity to actively promote abortion as a method of family planning shall not be attributed to an organization with which the individual is associated, provided that the individual is neither on duty nor acting on the organization's premises, and the organization neither endorses nor provides financial support for the action and takes reasonable steps to ensure that he or she does not improperly represent that the individual is acting on behalf of the organization.

Foreign contractor means a contractor or subcontractor organized or existing under the laws of a country other than the United States (the 50 states, the District of Columbia, and outlying areas). This excludes public international organizations.

Foreign nongovernmental organization means any nongovernmental organization or entity, whether non-profit or profit making, organized or existing under the laws of a country other than the United States (the 50 states, the District of Columbia, and outlying areas). This excludes public international organizations.

Global health assistance funding is Federal funding used for international health activities that is authorized under the Foreign Assistance Act of 1961, and funded from the Global Health Programs; Economic Support Fund; or Assistance for Europe, Eurasia, and Central Asia appropriations, including successor appropriations, under the annual Department of State, Foreign Operations, and Related Programs Appropriations Act. Global health assistance funding excludes funding for—

(1) Humanitarian assistance;

(2) U.S. Agency for International Development's (USAID's) American Schools and Hospitals Abroad Program activities;

(3) USAID's Food for Peace activities;

(4) USAID's Water Supply and Sanitation activities reported under Program Area HL.8 or successor program under the Department of State's Foreign Assistance Standardized Program Structure; and

(5) USAID's Vulnerable Children activities reported under Program Area ES 4.1 or successor program under the Department of State's Foreign Assistance Standardized Program Structure.

Perform abortions means to operate a facility where abortions are provided as a method of family planning. Excluded from this definition is the treatment of injuries or illnesses caused by legal or illegal abortions, for example, post-abortion care.

Provide financial support means to provide funding, from any source, to a foreign nongovernmental organization through a contract, subcontract, other written agreement or donation of funds; it does not include the provision of funding through contracts, subcontracts, or other written agreements for commercial items as defined under 2.101, except for commercial items to be used primarily to perform abortions as a method of family planning.

Public international organization means an organization—

(1) Designated as a public international organization under the International Organizations Immunities Act; or

(2) Treated as a public international organization pursuant to the regulations or policies of an Executive agency.

25.100X–5 Policy.

(a) The Protecting Life in Global Health Assistance policy is that executive agencies take appropriate actions to ensure that foreign nongovernmental organizations agree that they shall not perform or actively promote abortion as a method of family planning, nor provide financial support to any other foreign nongovernmental organization that conducts such activities, during the term of a contract funded with global health assistance funding. This policy applies to Federal assistance awards, as well as contracts containing the clause at 52.225–XX, Protecting Life in Global Health Assistance. For more information about the Protecting Life in Global Health Assistance policy, see the U.S. Agency for International Development's (USAID) website at *https://www.usaid.gov/global-health/legislative-policy-requirements.*

(b) To comply with the Protecting Life in Global Health Assistance policy, a foreign contractor or subcontractor is required to agree not to perform or actively promote abortion as a method of family planning or provide financial support to any other foreign nongovernmental organization that conducts such activities. U.S. contractors are required to flow this requirement down to all foreign subcontracts subject to this policy.

25.100X–6 Procedures.

(a) When the requiring activity notifies the contracting officer in writing that global health assistance funding is to be used for the procurement (see 7.10X), the contracting officer shall include the clause at 52.225–XX, Protecting Life in Global Health Assistance prescribed at 25.100X–7;

(b) When providing consent to subcontract with a foreign subcontractor in accordance with subpart 44.2, the contracting officer must ensure that the contractor has provided a description of the due diligence performed by the contractor on the subcontractor relating to the requirements in clause 52.225–XX (see 44.202–2(a)(14)).

25.100X–7 Contract clauses.

(a) Insert the clause at 52.225–XX, Protecting Life in Global Health Assistance, in solicitations and contracts that—

(1) Provide supplies or services for international health activities that are funded partially or wholly with global health assistance funding, including

contracts for technical assistance and training of foreign individuals or entities and services listed in 37.203(b)(1)–(6); and

(2) Are performed partially or wholly outside the United States (the 50 states, the District of Columbia, and outlying areas).

(b) The clause is not required to be used for—

(1) Contracts at or below the micro purchase threshold, as defined in FAR 2.101;

(2) Contracts for personal services with individuals; or

(3) Contracts for the acquisition of commercial items.

PART 44—SUBCONTRACTING POLICIES AND PROCEDURES

■ 5. Amend section 44.202–2 by adding paragraph (a)(14) to read as follows:

44.202–2 Considerations.

(a) * * *

(14) When the clause at 52.225–XX, Protecting Life in Global Health Assistance, is in the contract, has the contractor included a description of the due diligence performed on the subcontractor relating to the requirements of the clause.

* * * * *

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

■ 6. Add section 52.225–XX to read as follows:

52.225–XX Protecting Life in Global Health Assistance.

As prescribed in 25.100X–7, insert the following clause:

Protecting Life in Global Health Assistance (DATE)

(a) *Definitions.* As used in this clause–

Abortion as a method of family planning means abortion when it is for the purpose of spacing births. This includes, but is not limited to, abortions performed for the physical or mental health of the mother and abortions performed for fetal abnormalities, but does not include abortions performed if the life of the mother would be endangered if the fetus were carried to term, or abortions performed following rape or incest.

Actively promote abortion as a method of family planning means for an organization to commit resources, financial or other, in a substantial or continuing effort to increase the availability or use of abortion as a method of family planning.

(1) This includes, but is not limited to, the following activities:

(i) Operating a service-delivery site that provides, as part of its regular program, counseling, including advice and information, regarding the benefits and/or availability of abortion as a method of family planning;

(ii) Providing advice that abortion as a method of family planning is an available option or encouraging women to consider abortion (passively responding to a question regarding where a safe, legal abortion may be obtained is not considered active promotion if a woman who is already pregnant specifically asks the question, she clearly states that she has already decided to have a legal abortion, and the healthcare provider reasonably believes that the ethics of the medical profession in the host country requires a response regarding where it may be obtained safely and legally);

(iii) Lobbying a foreign government to legalize or make available abortion as a method of family planning or lobbying such a government to continue the legality of abortion as a method of family planning; and

(iv) Conducting a public information campaign outside the United States (the 50 states, the District of Columbia, and outlying areas), regarding the benefits and/or availability of abortion as a method of family planning.

(2) This does not include referrals for abortion as a result of rape or incest, or if the life of the mother would be endangered if she were to carry the fetus to term. Also excluded from this definition is the treatment of injuries or illnesses caused by legal or illegal abortions, for example, post-abortion care.

(3) Action by an individual acting in the individual's capacity to actively promote abortion as a method of family planning shall not be attributed to an organization with which the individual is associated, provided that the individual is neither on duty nor acting on the organization's premises, and the organization neither endorses nor provides financial support for the action and takes reasonable steps to ensure that he or she does not improperly represent that the individual is acting on behalf of the organization.

Foreign contractor means a contractor or subcontractor organized or existing under the laws of a country other than the United States (the 50 states, the District of Columbia, and outlying areas). This excludes public international organizations.

Foreign nongovernmental organization means any nongovernmental organization or entity, whether nonprofit or profit making, organized or existing under the laws of a country other than the United States (the 50 states, the District of Columbia, and outlying areas). This excludes public international organizations.

Full cooperation,

(1) Means, at a minimum—

(i) Disclosure to the Government information sufficient to identify the nature and extent of a violation;

(ii) Providing timely and complete responses to Government auditors' and investigators' requests for documents and access to employees with information; and

(iii) Cooperating fully in providing reasonable access to its facilities and staff (both inside and outside the U.S.) to allow contracting agencies and other responsible Federal agencies to conduct audits, investigations, or other actions to ascertain compliance with this clause.

(2) Does not—

(i) Foreclose any contractor rights arising in law, this regulation, or the terms of the contract;

(ii) Require the Contractor to waive its attorney-client privilege or the protections afforded by the attorney work product doctrine;

(iii) Require any officer, director, owner, employee, or agent of the Contractor, including a sole proprietor, to waive his or her attorney client privilege or Fifth Amendment rights; or

(iv) Restrict the Contractor from—

(A) Conducting an internal investigation; or

(B) Defending a proceeding or dispute arising under the contract or related to a potential or disclosed violation.

Global health assistance funding is Federal funding used for international health activities that is authorized under the Foreign Assistance Act of 1961, and funded from the Global Health Programs; Economic Support Fund; or Assistance for Europe, Eurasia, and Central Asia appropriations, including successor appropriations, under the annual Department of State, Foreign Operations, and Related Programs Appropriations Act. Global health assistance funding excludes funding for—

(1) Humanitarian assistance;

(2) U.S. Agency for International Development's (USAID's) American Schools and Hospitals Abroad Program activities;

(3) USAID's Food for Peace activities;

(4) USAID's Water Supply and Sanitation activities reported under Program Area HL.8 or successor program under the Department of State's Foreign Assistance Standardized Program Structure; and

(5) USAID's Vulnerable Children activities reported under Program Area ES 4.1 or successor program under the Department of State's Foreign Assistance Standardized Program Structure.

Parastatal means a foreign-government-owned organization operated as a commercial company or other organization, including nonprofits, or enterprises in which foreign governments or foreign agencies have a controlling interest.

Perform abortions means to operate a facility where abortions are provided as a method of family planning. Excluded from this definition is the treatment of injuries or illnesses caused by legal or illegal abortions, for example, post-abortion care.

Provide financial support means to provide funding, from any source, to a foreign nongovernmental organization through a contract, subcontract, other written agreement or donation of funds; it does not include the provision of funding through contracts, subcontracts, or other written agreements for commercial items as defined under 2.101, except for commercial items to be used primarily to perform abortions as a method of family planning.

Public international organization means an organization—

(1) Designated as a public international organization under the International Organizations Immunities Act; or

(2) Treated as a public international organization pursuant to the regulations or policies of an Executive agency.

(b) *Prime contractor.* The Contractor shall not subcontract for supplies or services using global health assistance funding under this contract with a foreign contractor unless the subcontractor at any tier agrees, by entering into such subcontract, that it shall not, during the term of the subcontract—

(1) Perform or actively promote abortion as a method of family planning, outside the United States (the 50 states, the District of Columbia, and outlying areas); or

(2) Provide financial support to any other foreign nongovernmental organization that conducts such activities.

(c) *Foreign prime contractors.* This paragraph (c) applies only to foreign prime contractors, and does not affect any contractual rights between U.S. prime contractors and the U.S. Government:

(1) The Contractor shall not, during the term of this contract—

(i) Perform or actively promote abortion as a method of family planning outside the United States (the 50 states, the District of Columbia, and outlying areas); or

(ii) Provide financial support to any other foreign nongovernmental organization that conducts such activities.

(2) The Contractor shall allow authorized representatives of the Government to, at any reasonable time, announced or unannounced, consistent with the terms of this contract—

(i) Inspect the documents and materials maintained or prepared by the Contractor in the usual course of its operations that describe the health activities implemented by the Contractor, including reports, brochures, and service statistics;

(ii) Observe the health activities conducted by the Contractor;

(iii) Consult with healthcare personnel of the Contractor; and

(iv) Obtain a copy of audited financial statements or reports of the Contractor; as applicable.

(3) The Government shall terminate the performance of work under this contract in accordance with the termination clause of this contract for any violation of this clause unless the Government determines that other corrective action or remedy is warranted. In addition to other remedies available to the Government, the Contractor's failure to comply with the requirements of this clause may result in—

(i) Suspension of contract payments until the Contractor has taken appropriate remedial action; and/or

(ii) Suspension or debarment.

(d) *Subcontractor eligibility.* When the Contractor is determining whether a foreign contractor is eligible for a subcontract with global health assistance funding under this contract, the action of separate nongovernmental organizations shall not be imputed to the subcontractor, unless, in the judgment of the Government, a separate nongovernmental organization is being used purposefully to avoid the requirements of the clause.

(1) Separate nongovernmental organizations are those that have distinct legal existence in accordance with the laws of the countries in which they are organized. Foreign organizations that are separately organized shall not be considered separate if they are affiliates (see definition at FAR 2.101).

(2) The Contractor may request the Government's approval to treat as separate the health activities of two or more organizations, which would be considered affiliates under paragraph (d)(1) of this clause.

(3) In the event the Contractor makes a request under paragraph (d)(2) of this clause, the Contractor shall provide a written justification to the Government that the health activities of the organizations are sufficiently distinct to warrant not imputing the activity of one to the other.

(e) *Consent to subcontract.* If the contract includes the clause at FAR 52.244–2, Subcontracts, and requires the Contractor to obtain consent prior to entering into a subcontract, then the Contractor shall provide to the Contracting Officer, in the consent request, a description of the due diligence performed by the Contractor on the subcontractor relating to the requirements in this clause.

(f) *Violations.* Violations by the subcontractor of any requirement in this clause will be imputed to the Contractor only if—

(1) The Contractor knowingly provides global health assistance funding in a subcontract under this contract to a foreign contractor that performs or actively promotes abortion as a method of family planning;

(2) The Contractor failed to make reasonable due diligence efforts prior to providing global health assistance funding in a subcontract under this contract to a foreign contractor, and the subcontractor did not abide by its contractual terms required in this clause; or

(3) The Contractor knows or has reason to know, by virtue of the monitoring that the contractor is required to perform under the terms of this contract, that a subcontractor has violated any of the contract terms required by this clause, and the Contractor fails to terminate the subcontract or fails to take other appropriate corrective action.

(g) *Government independent inquiries.* (1) The Government may make independent inquiries in the community served by a foreign contractor or subcontractor under this contract regarding whether it performs or actively promotes abortion as a method of family planning.

(2) In the event that the Contractor or the Government has reason to believe that a foreign subcontractor may have violated the requirements of this clause, the Contractor shall review the health program of the foreign subcontractor to determine whether such a violation has occurred. The Contractor shall provide the Contracting Officer the results of the review.

(h) *Foreign Governments and parastatals.* The Contractor may award a contract with global health assistance funding to a foreign government or parastatal even though the foreign government or parastatal includes abortion in its health program, provided that no global health assistance funding shall be used under this contract in support of the abortion activity of the foreign government or parastatal, and any funds transferred to the foreign government or parastatal shall be placed in a segregated account to ensure that such funds are not used to support the abortion activity of the foreign government or parastatal.

(i) *Affirmative duty exception.* In the event of a conflict between a term of this clause and an affirmative duty of a healthcare provider required under local law to provide counseling about and referrals for abortion as a method of family planning, compliance with such law shall not trigger a violation of this clause.

(j) *Obligations regarding foreign subcontracts.* (1) The Contractor shall ensure that foreign subcontractors at any tier that receive global health assistance funding agree to the following additional terms:

(i) The subcontractor shall not, during the term of the subcontract

(A) Perform or actively promote abortion as a method of family planning outside the United States (the 50 states, the District of Columbia, and outlying areas); or

(B) Provide financial support to any other foreign nongovernmental organization that conducts such activities.

(ii) The Contractor and authorized representatives of the Government may, at any reasonable time, announced or unannounced, consistent with the terms of this contract, perform any of the following:

(A) Inspect the documents and materials maintained or prepared by the subcontractor in the usual course of its operations that describe the health activities of the subcontractor, including reports, brochures, and service statistics.

(B) Observe health activities conducted by the subcontractor.

(C) Consult with healthcare personnel of the subcontractor.

(D) Obtain a copy of audited financial statements or reports of the subcontractor, as applicable.

(2) In the event that the Contractor or the Government has reason to believe that a foreign subcontractor may have violated the requirements of this clause, the Contractor shall review the health program of the subcontractor to determine whether such a violation has occurred.

(3) If the Contractor has reason to believe that the subcontractor has violated any requirement of this clause, the Contractor shall consult with the Contracting Officer and provide full cooperation prior to terminating the subcontract or determining that other corrective action is warranted.

(k) *Subcontracts.* The Contractor shall insert the terms of this clause, except paragraphs (b), (c) and (e), in all subcontracts awarded with global health assistance funding at any tier except for subcontracts—

(1) At or below the micro-purchase threshold, as defined at FAR 2.101;

(2) For personal services with individuals; or

(3) For the acquisition of commercial items.

(End of Clause)

[FR Doc. 2020–17551 Filed 9–10–20; 1:30 pm]

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DEPARTMENT OF DEFENSE

GENERAL SERVICES ADMINISTRATION

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

48 CFR Parts 12, 25, and 52

[FAR Case 2019–016; Docket No. FAR–2019–0016, Sequence No. 1]

RIN 9000–AN99

Federal Acquisition Regulation: Maximizing Use of American-Made Goods, Products, and Materials

AGENCY: Department of Defense (DoD), General Services Administration (GSA), and National Aeronautics and Space Administration (NASA).

ACTION: Proposed rule.

SUMMARY: DoD, GSA, and NASA are proposing to amend the Federal Acquisition Regulation (FAR) to implement an Executive order (E.O.) addressing domestic preferences in Government procurement.

DATES: Interested parties should submit written comments at the address shown below on or before November 13, 2020 to be considered in the formation of the final rule.

ADDRESSES: Submit comments in response to FAR Case 2019–016 to *http://www.regulations.gov.* Submit comments via the Federal eRulemaking portal by searching for ''FAR Case 2019–016''. Select the link ''Comment Now'' that corresponds with ''FAR Case 2019–016.'' Follow the instructions provided on the screen. Please include your name, company name (if any), and ''FAR Case 2019–016'' on your attached document. If your comment cannot be submitted using *https://www.regulations.gov,* call or email the points of contact in the **FOR FURTHER INFORMATION CONTACT** section of this document for alternate instructions.

Instructions: Please submit comments only and cite ''FAR Case 2019–016'' in all correspondence related to this case. All comments received will be posted without change to *http://www.regulations.gov,* including any personal and/or business confidential information provided. To confirm receipt of your comment(s), please check *https://www.regulations.gov,* approximately two to three days after submission to verify posting.

FOR FURTHER INFORMATION CONTACT: Ms. Zenaida Delgado, Procurement Analyst, at 202–969–7207 or *zenaida.delgado@gsa.gov* for clarification of content. For information pertaining to status or publication schedules, contact the Regulatory Secretariat Division at 202–501–4755 or *GSARegSec@gsa.gov.* Please cite FAR Case 2019–016.

SUPPLEMENTARY INFORMATION:

I. Background

Congress passed the Buy American Act during the Great Depression to foster American industry by protecting it from foreign competition for Federal procurement contracts. The Buy American Act is codified at 41 U.S.C. Chapter 83 as the Buy American statute and provides pricing preferences to offerors who certify their compliance with the domestic purchasing requirements stated in the Act. Specifically, it requires public agencies to procure articles, materials, and supplies that were mined, produced, or manufactured in the United States, substantially all from domestic components, subject to exceptions for nonavailability of domestic products, unreasonable cost of domestic products, and when it would not be in the public interest to buy domestic products.

The key to understanding the Buy American statute, which is implemented in FAR part 25, is determining whether the solicited goods or ''end products'' or ''construction material'' are domestic, *i.e.,* were mined, produced, or manufactured in the United States, substantially from components mined, produced, or manufactured in the United states. The analysis of whether a manufactured end product or construction material qualifies as domestic is done using a two-part test.

1. The end product or construction material must be manufactured in the United States.

2. More than 50 percent of all component parts (determined by cost of the components) must also be mined, produced, or manufactured in the United States.

The factor of 50 percent in the existing FAR definition came from E.O. 10582, Prescribing Uniform Procedures for Certain Determinations under the Buy American Act, available via the internet at *https://www.archives.gov/federal-register/codification/executive-order/10582.html.* E.O. 10582 interpreted the statutory requirement that domestic products must be manufactured ''substantially all'' from domestic components as meaning in excess of 50 percent. If a product meets this two-part test, then it can be considered a ''domestic end product'' or ''domestic construction material'' under the Buy American statute. End products or construction material that do not qualify as domestic under this test are treated as foreign.

The Buy American statute is waived in situations where the United States has reciprocal trade agreements, including the World Trade Organization Government Procurement Agreement (WTO GPA). Generally, the dollar value of the acquisition determines which of the trade agreements applies. Exceptions to the applicability of the trade agreements are described in FAR subpart 25.4. The FAR clauses implementing the Trade Agreements Act allow the Government to purchase end items that are ''substantially transformed'' in countries that are parties to such trade agreements without regard to the source or cost of the components. On acquisitions under the WTO GPA, end products that are ''substantially transformed'' in the United States are considered ''U.S.-made end products'' and they are not subject to the Buy American statute or E.O. 13881.

On July 15, 2019, the President signed E.O. 13881, Maximizing Use of American-Made Goods, Products, and Materials (84 FR 34257, July 18, 2019). This E.O. changes FAR clauses implementing the Buy American statute by increasing the—

1. Domestic content requirements; and

2. Price preference for domestic products.

Increased Domestic Content Requirements

Under E.O. 13881, the domestic content requirement for iron and steel end products increases to 95 percent. For everything else, the domestic content requirement increases from 50 percent to exceeds 55 percent of the cost of all components. E.O. 13881 creates a new separate higher domestic content standard for iron and steel end products. This distinction does not currently appear in the FAR clauses implementing the Buy American statute. But it has been around for many years in domestic preference requirements governing certain federal grant programs, such as the Federal Transit Administration's Buy America regulations applicable to grantees. DoD procurements are affected by the increased domestic content requirements of E.O. 13881; the changes will be implemented in the Defense Federal Acquisition Regulation Supplement (DFARS) through DFARS Case 2019–D045, Maximizing Use of American-Made Goods.

Increase Preference for Domestic Offers

The Buy American statute does not prohibit the purchase of foreign end products or use of foreign construction material. Instead, it encourages the use of domestic end products and construction material by imposing a price preference for domestic end products and construction material. Under current Buy American regulations, large businesses receive a 6 percent price preference. Small businesses get a 12 percent price preference. For DoD procurements, the price preference for end products from both large and small businesses is 50 percent. The 6 percent price preference was originally established by E.O. 10582, which permitted the head of an executive agency to determine that a greater differential is appropriate. In October 1958, the Assistant Secretary of Defense (Supply and Logistics) and the Assistant Secretary of State agreed that a differential of 12 percent would be used for offers from small business (see Armed Services Procurement Regulation (ASPR), 1955 edition, Revision 45, 20 April 1959, Case 58–99).

E.O. 13881 increases the price preference from 6 percent to 20 percent for large businesses and from 12 percent to 30 percent for small businesses. The E.O. does not impact the 50 percent preference for DoD procurements, because the DoD percentage exceeds the requirements of the E.O.

II. Discussion and Analysis

A. Applicability of the Executive Order 13881 to Construction Material

Although the E.O. addresses only ''end products'' in section 2, the Councils have interpreted the term ''end product'' in the E.O. to include ''construction material.'' The E.O. doesn't define the term end product, but in both the title and section 1, addresses maximizing the use of American-made goods, products, and materials, not just end products. Furthermore, section 3 of the E.O. states that it will supersede section 2(a) of E.O. 10582, which addressed ''materials,'' and has been interpreted in the FAR to cover both end products and construction materials. In addition, the policy relating to iron and steel products has primary impact on the acquisition of construction materials. The Recovery Act applied the restrictions on acquisition of domestic iron and steel products solely to construction materials (see FAR subpart 25.6). Not addressing construction material in this rule would be contrary to the goal of the E.O. to maximize the use of American-made products.

B. Definitions

1. This rule proposes to amend the definitions of ''domestic construction material'' and ''domestic end product'' at FAR 25.003 and in the applicable clauses at FAR 52.225–1, 52.225–3, 52.225–9, and 52.225–11, and references at FAR 52.212–3(f)(1) and (g)(1)(iii), 52.225–2(a), and 52.225–4(c), as well as the policy discussion of these definitions at FAR 25.001(c)(1), 25.101(a)(2), and 25.201(b), to include the new E.O. requirement that for ''domestic construction material'' or a ''domestic end product'' that does not consist wholly or predominantly of iron or steel or a combination of both, the cost of domestic components must exceed 55 percent of the cost of all components.

2. A new paragraph is added in each definition to address end products or construction materials that consist wholly or predominantly of iron or steel or a combination of both, respectively, to require that the cost of iron and steel not produced in the United States as estimated in good faith by the contractor, must constitute less than 5 percent of the cost of all components. This addition to the definitions was derived and integrated with existing FAR coverage as follows:

a. Iron and steel end product means an end product or construction material that consists wholly or predominantly of iron or steel or a combination of both.

b. Predominantly of iron or steel or a combination of both means the cost of the iron and steel content in an item that exceeds 50 percent of the total cost of all its components. Basing the predominance on cost, rather than weight, is consistent with the requirement of the E.O. that the foreign iron and steel content be limited to less than 5 percent of the cost of all components.

c. Foreign iron and steel means iron and steel not produced in the United States. This is consistent with the definition of ''foreign iron and steel'' under the Recovery Act (see FAR 25.602–1(a)(1)(ii)).

d. When addressing construction materials or end products that are wholly or predominantly iron or steel or a combination of both, it is unnecessary to address unmanufactured construction material or unmanufactured end products, respectively, because the Government does not buy unmanufactured iron and steel end products and construction materials.

e. ''Produced in the United States'' is taken from FAR subpart 25.6, and applies to the iron and steel in construction material and end products that consist wholly or predominantly of iron or steel or a combination of both.

f. The definition of ''steel'' is taken from FAR subpart 25.6.

g. Because of the difficulty of estimating the cost of all foreign iron and steel content, the rule proposes a good faith estimate by the contractor, with the exception of fasteners, which, as explained in section II.C., are defined and treated separately.

h. The requirement that components of unknown origin be treated as foreign has been incorporated into the definitions of ''domestic end product'' and ''domestic construction material'' for those items that do not consist wholly or predominantly of iron or steel or a combination of both. This requirement is comparable to the other requirements already in the definition such as the treatment of domestically nonavailable components and scrap generated in the United States as domestic. This makes it clearer that this is only applicable to items that do not consist wholly or predominantly of iron or steel or a combination of both.

i. The rule revises the term ''component test'' to ''domestic content test,'' which can apply to either the component content of other than iron or steel products test, or the iron and steel content of iron or steel products, as applicable. With regard to manufactured supplies and materials (whether end products or construction materials), the Buy American statute requires that in order to be considered domestic, such materials and supplies shall have been manufactured in the United States ''substantially all from articles, materials, or supplies mined produced, or manufactured in the United States.''

E.O. 10582 interpreted this requirement by stating that materials shall be considered to be of foreign origin if the cost of foreign products used in such materials constitutes 50 percent or more of the cost of all the products used in such materials. When incorporated into the FAR, the term ''component'' was substituted for the term ''product'' and this has been referred to as the ''component test''. Although E.O. 13881 retains similar language with regard to end products other than iron and steel end products, just changing the percentage from 50 percent to 45 percent, E.O. 13881 does not reference the term ''product'' when referring to the cost of iron and steel used in iron and steel end products. It states that ''the cost of foreign iron and steel used in such iron and steel end products constitutes 5 percent or more of the cost of all the products used in such iron and steel end products.'' Thus, the test for iron and steel is no longer a ''component test'' but a test of the cost of iron and steel content.

C. Partial Reinstatement of the Domestic Content Test of the Buy American Statute for Iron and Steel Products

In 2009, the Administrator for Federal Procurement Policy waived what is now called the domestic content test (previously called the component test) for commercially available off-the-shelf (COTS) items based on a determination made pursuant to 41 U.S.C. 1907. See FAR Case 2000–305, January 15, 2009, 74 FR 2713. Furtherance of the Buy American statute was driven by retention of the requirement that the product must still be manufactured in the United States.

The proposed rule would partially restore the domestic content test for COTS items as it pertains to iron and steel products. The bulk of iron and steel products acquired by the Government are primarily COTS items, used as construction material. Roll-back of the waiver is necessary to give full effect to the E.O.'s requirement that domestic iron and steel products shall not contain more than 5 percent foreign iron and steel.

At the same time, the proposed rule would continue to waive the domestic content test for iron and steel fasteners. Fastener is defined as a hardware device that mechanically joins or affixes two or more objects together. Examples of fasteners are nuts, bolts, pins, rivets, nails, clips, and screws. Fasteners are generally so small, inexpensive and comingled that trying to keep track of the origin of all fasteners would create an administrative burden that would outweigh any benefit to the American iron and steel industrial base. The proposed partial reinstatement of the domestic content test for products that consist wholly or predominantly of iron or steel or a combination of both would require changes to the list of inapplicable laws at FAR 12.505(a), the definitions of ''domestic construction material'' and ''domestic end product,'' and various other conforming changes wherever waiver of the now domestic content test is mentioned (FAR 25.001(c)(1), 25.100(a)(4), 25.101(a)(2), 25.200(a)(4), 25.201(b)(2), 52.225–1(b), 52.225–3(c), 52.225–9(b), and 52.225–11(b)).

D. Evaluation Factor for Determination of Unreasonable Cost

The new E.O. also increases the evaluation factors to be applied to offers of foreign end products or construction material when determining whether the cost of offered domestic end products or construction material is unreasonable. For acquisitions of end products, the factor of 20 percent is to be applied to a foreign offer if the potential domestic awardee is other than a small business, and a 30 percent factor is to be applied if the potential awardee would be a small business (see FAR 25.105(b), 25.204, 25.502(c), 25.604, 25.605, 52.225–9(b)(3)(i), 52.225–11((b)(4)(i), and the Recovery Act clauses at 52.225–21 through 52.225–24). Consistent with current FAR coverage for acquisitions of foreign construction material under a construction contract, the higher preference for small businesses is inapplicable, because under a construction contract, there are not separately identifiable offers on each item of construction material, but it is part of an overall bid on the project. The foreign material is evaluated on the basis of market research, not a specific competing offer. Thus, only the 20 percent factor would be applied to construction material.

E. Applicability to Acquisitions Funded by the Recovery Act

Projects funded with monies from section 1605 of the American Recovery and Reinvestment Act of 2009 (the Recovery Act) (Pub. L. 111–5) are subject to more stringent requirements for use of domestic manufactured construction material, particularly iron and steel (see FAR subpart 25.6). The Recovery Act restrictions apply only to construction projects using funds appropriated under that Act. Most of those funds have now been obligated and expended, and there is very little continued applicability of these regulations.

The Recovery Act does not apply to unmanufactured construction material, which is therefore still covered by the Buy American statute. The increased requirements of the new E.O. for domestic content for manufactured construction material are therefore inapplicable to acquisitions under the Recovery Act.

However, the 20 percent factor that applies to construction contracts covered by the Buy American statute, only applies to the unmanufactured construction material of a construction contract otherwise covered by the Recovery Act. Accordingly, the 6 percent factor is revised to 20 percent at FAR 25.604(c)(2) and 25.605 and in the following Recovery Act provisions and clause:

52.225–21, Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials.

52.225–22, Notice of Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials.

52.225–23, Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials Under Trade Agreements.

52.225–24, Notice of Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials Under Trade Agreements.

III. Applicability to Contracts at or Below the Simplified Acquisition Threshold (SAT) and for Commercial Items, Including Commercially Available Off-the-Shelf (COTS) Items

This proposed rule does not add any new provisions or clauses, nor change the applicability of existing provisions or clauses to contracts at or below the SAT and contracts for the acquisition of commercial items, including COTS items.

However, this rule does propose to apply the domestic content test of the Buy American statute, as implemented by E.O. 13881, to COTS items that consist wholly or predominantly of iron and steel (excluding fasteners). In accordance with 41 U.S.C. 1907, since 2008, the domestic content test of the Buy American statute has been waived for COTS items, in part due to the complexity and cost of keeping track of components in a world of global sourcing where the Government is not a market driver. However, the domestic content test for the iron and steel items does not require tracking of all components, only a good faith assurance that not more than 5 percent of the iron and steel content is foreign. In addition, absent restoration of the domestic content test, the E.O. 13881 requirement with regard to iron and steel construction material would have very little effect.

As explained above, the domestic content waiver for COTS items would continue to apply to iron and steel fasteners, such as nuts, bolts, pins, rivets, nails, clips, and screws, which are generally so small, inexpensive and comingled that trying to keep track of the origin of all fasteners would create an administrative burden that would outweigh any benefit to the American iron and steel industrial base.

IV. Executive Orders 12866 and 13563

Executive Orders (E.O.s) 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). E.O. 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. This is a significant regulatory action and, therefore, was subject to review under section 6(b) of E.O. 12866, Regulatory Planning and Review, dated September 30, 1993. This rule is not a major rule under 5 U.S.C. 804.

V. Expected Impact of the Proposed Rule

The current FAR clauses implementing the Buy American statute apply to a narrow set of procurements. Also, because the FAR Council is leaving the COTS items exception in place for most COTS items, the heightened domestic content requirements will not be applicable to those procurements.

When this rule is implemented, domestic industries supplying domestic end products are likely to benefit from a competitive advantage. Based on the E.O., it is unclear if the pool of qualified suppliers would be reduced, resulting in less competition (and a possible increase in prices that the Government will pay to procure these products).

At least three arguments point to the possibility that any increased burden, on contractors in particular, could be small if not de minimis: (1) Familiarization costs should be low, (2) some, if not many, contractors may already be able to meet the more stringent threshold, and (3) costs incurred by contractors who adjust their supply chains so that their end products qualify as domestic will enjoy a larger price preference that should help to offset these costs over time. Each of these arguments is explained below.

First, DoD, GSA, and NASA do not anticipate significant cost from contractor familiarization with the rule given the history of rulemaking and E.O.s in this area. The basic mechanics of the Buy American statute (*e.g.,* definitions, how and when the price preference is used to favor domestic end products, certifications required of offerors to demonstrate end products are domestic) remain unchanged and continue to reflect processes that are decades old.

Second, some, if not many, contractors may already be able to comply with the lower foreign content requirement needed to meet the definition of domestic end product under E.O. 13881 and the proposed rule. Laws such as the SECURE Technology Act, Public Law 115–390, which requires a series of actions to strengthen the Federal infrastructure for managing supply chain risks, are placing significantly increased emphasis on Federal agencies and Federal Government contractors to identify and reduce risk in their supply chains. One way to reduce supply chain risk is to increase domestic sourcing of content. In addition, in the context of iron and steel, many laws already in place call for more stringent content. For example, the Recovery Act required that all construction material for a project for the construction, alteration, maintenance, or repair of a public building or a public work in the United States, consisting wholly or predominantly of iron or steel, had to be produced in the United States when using Recovery Act funds, to the extent consistent with trade agreements (see FAR 25.602–1, implementing section 1605 of the Recovery Act). In addition, Federal contractors who also work on contracts funded under Federal grants may, in some cases, find that the steel, iron, and manufactured goods used in the project be produced in the United States, as is the case for certain funding administrated by the Federal Transit Administration for public transportation projects (see 49 U.S.C. 5323(j)). Accordingly, it is possible that the Federal market for iron and steel has already done significant retooling and could meet the requirements of E.O. 13881 without too much additional effort.

Third, it is anticipated that some contractors' products and construction materials may not meet the definition of domestic end product and construction material unless the contractors take steps to adjust their supply chains to increase the domestic content. Those contractors that make a business decision not to modify their supply chains will still be able to bid on Federal contracts but will no longer enjoy a price preference. Those contractors that sell to civilian agencies and retool their supply sources to meet the more stringent threshold will have a more generous price preference applied to their products—*i.e.,* 20 percent generally under the new rule vs. 6 percent under the current rule; 30 percent if the seller is a small business vs. 12 percent under the current rule. These stronger preferences, which are designed as an incentive to encourage more domestic sourcing, may help to offset costs of meeting the new standards.

This rule has the potential to slightly increase the estimated percentage of foreign offers. It can only impact products that are made in the United States as follows: Iron or steel that has a content of 5 percent or more of foreign iron or steel; or other products, other than COTS items, that have a content of 45 to 50 percent foreign components. Offerors of such products have an option to increase the domestic content and continue to offer domestic products, in which case they may benefit from the increased preference for domestic products, or they may choose to continue to offer the same product, which will now be evaluated as foreign. We do not have any data on how many currently domestic products would fall into this category. Nor do we have any knowledge as to which option an offeror of such products would select. With regard to the increased price preference for domestic offers, we note that robust competition among vendors offering domestic products will decrease the extent to which the Government could pay an additional 20 to 30 percent for domestic products above and beyond the cost of otherwise equivalent foreign products.

DoD, GSA, and NASA do not expect a significant cost impact on the public but lack data to make a definitive determination and seek information from the public to assist with this analysis. Feedback is requested on the following questions:

(1) What industry do you represent? Are you a manufacturer or a reseller?

(2) For manufacturers and resellers of end products other than iron and steel—

(a) Do you currently meet the higher standards specified in the proposed rule for a domestic end product or construction material or would you have to make adjustments to your supply chain to meet the new requirements?

(b) If you would have to make adjustments to your supply chain in response to changes proposed here, do you plan to do so?

(c) If the answer to question (b) is yes, how much do you think it will cost to make these changes, and to what extent do you believe this cost will be offset by the increased preference applicable to purchases by civilian agencies if you move toward products with higher domestic content?

(3) For sellers of iron and steel, what, if any, adjustments do you anticipate having to make to your supply chain to meet the new requirements, and how much do acquisition costs vary between iron and steel with less or equal than 95 percent domestic content, and greater than 95 percent domestic content?

(4) Section 4 of E.O. 13881 directed consideration of the ''feasibility and desirability'' of further decreases in the threshold percentage of foreign content allowed for an end product other than

iron or steel to be considered domestic from the 45 percent proposed in this rule to 25 percent. Accordingly, DoD, GSA, and NASA encourage manufacturers and resellers of end products other than iron and steel to provide input on the feasibility and desirability of adopting this more stringent standard by addressing the following—

(a) Could you currently meet a 25 percent foreign content requirement for domestic end products or construction material or would you have to make adjustments to your supply chain to do so?

(b) If you would have to make adjustments to your supply chain to meet a 25 percent requirement, would you do so?

(c) If the answer to question (b) is yes, how much do you think it would cost to come into compliance, how much would acquisition costs for these materials rise, and to what extent do you believe this cost would be offset by the increased preference applicable to purchases by civilian agencies?

(d) Do you think it is preferable to work towards a 25 percent threshold incrementally? If so, why and what incremental change would you propose over what period of time?

VI. Executive Order 13771

DoD, GSA, and NASA do not expect this to be considered a regulatory action under E.O. 13771, Reducing Regulation and Controlling Regulatory Costs, because this rule is expected to have a de minimis burden impact on the public (see section V of this preamble).

VII. Regulatory Flexibility Act

DoD, GSA, and NASA do not expect this rule to have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act, 5 U.S.C. 601, *et seq.,* because this rule does not impose new requirements just changes to the existing percentages. This rule proposes to make adjustments to the required percentage of domestic content and the existing percentages for the price evaluation preferences in an effort to decrease the amount of foreign-sourced content in a U.S. manufactured product to promote economic and national security, help stimulate economic growth, and create jobs.

Nevertheless, an Initial Regulatory Flexibility Analysis (IRFA) has been performed and summarized as follows:

This case amends the FAR to implement an Executive order regarding maximizing the use of American-made goods, products, and materials.

The objective of this proposed rule is to strengthen domestic preferences under the Buy American statute, as required by E.O. 13881, by changing how a domestic product is defined and how the price of a domestic product is determined to be unreasonable.

In accordance with Federal Procurement Data System data for fiscal years (FY) 2017, 2018, and 2019 for new awards with foreign place of performance for construction valued over the micro-purchase threshold and awards for supplies to unique small businesses; this rule will apply to only the 8 percent of foreign construction awards which were made to small businesses and, only 14 percent of foreign supply awards were made to small businesses.

Buy American statute	FY 2017	FY 2018	FY 2019	Median
	SB/Total	SB/Total	SB/Total	SB %
Construction	18/217 = 8%	13/223 = 6%	15/199 = 8%	8%
Supplies	153/1,200 = 13	164/1,161 = 14	164/1,048 = 16	14

This rule is covered under the existing information collection requirements associated with the Buy American statute. The rule will strengthen domestic preferences under the Buy American statute and provide small businesses the opportunity and incentive to deliver U.S. manufactured products from domestic suppliers. It is expected that this rule will benefit U.S. small business manufacturers, including those of iron or steel.

This rule does not duplicate, overlap, or conflict with any other Federal rules.

DoD, GSA, and NASA were unable to identify any significant alternatives.

The Regulatory Secretariat Division has submitted a copy of the IRFA to the Chief Counsel for Advocacy of the Small Business Administration. A copy of the IRFA may be obtained for the Regulatory Secretariat Division. DoD, GSA, and NASA invite comments from small business concerns and other interested parties on the expected impact of this rule on small entities.

DoD, GSA, and NASA will also consider comments from small entities concerning the existing regulations in subparts affected by the rule in accordance with 5 U.S.C. 610. Interested parties must submit such comments separately and should cite 5 U.S.C 610 (FAR Case 2019–016), in correspondence.

VIII. Paperwork Reduction Act

The Paperwork Reduction Act (44 U.S.C. chapter 35) does apply; however, these changes to the FAR do not impose additional information collection requirements to the paperwork burden previously approved under the Office of Management and Budget Control Number 9000–0024, Buy American, Trade Agreements, and Duty-Free Entry-FAR Sections Affected: 52.225–2; 52.225–4, 52.225–6, 52.225–8 thru 52.225–12, and 52.225–21 & 52.225–23.

List of Subjects in 48 CFR Parts 12, 25, and 52

Government procurement.

William F. Clark,

Director, Office of Government-wide Acquisition Policy, Office of Acquisition Policy, Office of Government-wide Policy.

Therefore, DoD, GSA, and NASA propose amending 48 CFR parts 12, 25, and 52 as set forth below:

■ 1. The authority citation for 48 CFR parts 12, 25, and 52 continues to read as follows:

Authority: 40 U.S.C. 121(c); 10 U.S.C. chapter 137; and 51 U.S.C. 20113.

PART 12—ACQUISITION OF COMMERCIAL ITEMS

■ 2. Amend section 12.505 by revising paragraph (a) to read as follows:

12.505 Applicability of certain laws to contracts for the acquisition of COTS items.

* * * * *

(a)(1) The portion of 41 U.S.C. 8302, American Materials Required for Public Use, paragraph (a)(1) that reads ‘‘substantially all from articles, materials, or supplies mined, produced, or manufactured in the United States,’’ Buy American—Supplies, domestic content test, except as provided in 25.101(a)(2)(ii) (see 52.225–1 and 52.225–3).

(2) The portion of 41 U.S.C. 8303, Contracts for Public Works, paragraph (a)(2) that reads ‘‘substantially all from articles, materials, or supplies mined, produced, or manufactured in the United States,’’ Buy American—Construction Materials, domestic content test, except as provided in 25.201(b)(2)(ii)(see 52.225–9 and 52.225–11).

* * * * *

PART 25—FOREIGN ACQUISITION

■ 3. Amend section 25.001 by revising paragraph (c)(1) to read as follows:

25.001 General.

* * * * *

(c) * * *

(1) The Buy American statute uses a two-part test to define a ''domestic end product'' or ''domestic construction material'' (manufactured in the United States and a domestic content test). The domestic content test has been waived for acquisition of commercially available off-the-shelf items, except a product that consists wholly or predominantly of iron or steel or a combination of both (excluding fasteners) (see 25.101(a) and 25.201(b)).

* * * * *

■ 4. Amend section 25.003 by—

■ a. Revising the definitions ''Domestic construction material'' and ''Domestic end product''; and

■ b. Adding in alphabetical order the definitions ''Fastener'', ''Predominantly of iron or steel or a combination of both'', and ''Steel''.

The revisions and additions read as follows:

25.003 Definitions.

* * * * *

Domestic construction material means—

(1) For use in subparts other than 25.6—

(i) For construction material that does not consist wholly or predominantly of iron or steel or a combination of both—

(A) An unmanufactured construction material mined or produced in the United States; or

(B) A construction material manufactured in the United States, if—

(*1*) The cost of the components mined, produced, or manufactured in the United States exceeds 55 percent of the cost of all its components. Components of foreign origin of the same class or kind for which nonavailability determinations have been made are treated as domestic. Components of unknown origin are treated as foreign; or

(*2*) The construction material is a COTS item; or

(ii) For construction material that consists wholly or predominantly of iron or steel or a combination of both, a construction material manufactured in the United States if the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, constitutes less than 5 percent of the cost of all the components used in such construction material (produced in the United States means that all manufacturing processes of the iron or steel must take place in the United States, except metallurgical processes involving refinement of steel additives); or

(2) For use in subpart 25.6, see the definition in 25.601.

Domestic end product means—

(1) For an end product that does not consist wholly or predominantly of iron or steel or a combination of both—

(i) An unmanufactured end product mined or produced in the United States;

(ii) An end product manufactured in the United States, if—

(A) The cost of its components mined, produced, or manufactured in the United States exceeds 55 percent of the cost of all its components. Components of foreign origin of the same class or kind as those that the agency determines are not mined, produced, or manufactured in sufficient and reasonably available commercial quantities of a satisfactory quality are treated as domestic. Components of unknown origin are treated as foreign. Scrap generated, collected, and prepared for processing in the United States is considered domestic; or

(B) The end product is a COTS item; or

(2) For an end product that consists wholly or predominantly of iron or steel or a combination of both, an end product manufactured in the United States, if the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, constitutes less than 5 percent of the cost of all the components used in the end product (produced in the United States means that all manufacturing processes of the iron or steel must take place in the United States, except metallurgical processes involving refinement of steel additives).

* * * * *

Fastener means a hardware device that mechanically joins or affixes two or more objects together. Examples of fasteners are nuts, bolts, pins, rivets, nails, clips, and screws.

* * * * *

Predominantly of iron or steel or a combination of both means that the cost of the iron and steel content in an item exceeds 50 percent of the total cost of all its components.

Steel means an alloy that includes at least 50 percent iron, between .02 and 2 percent carbon, and may include other elements.

* * * * *

■ 5. Amend section 25.100 by—

■ a. Removing from the end of paragraph (a)(2) ''and'';

■ b. Redesignating paragraph (a)(3) as paragraph (a)(4);

■ c. Adding a new paragraph (a)(3); and

■ d. Revising the newly redesignated paragraph (a)(4).

The addition and revision read as follows:

25.100 Scope of subpart.

(a) * * *

(3) Executive Order 13881, July 15, 2019; and

(4) Waiver of the domestic content test of the Buy American statute for acquisition of commercially available off-the-shelf (COTS) items in accordance with 41 U.S.C. 1907, but see 25.101(a)(2)(ii).

* * * * *

■ 6. Amend section 25.101 by—

■ a. Removing from paragraph (a) introductory text ''statute uses'' and adding ''statute and E.O. 13881 use'' in its place;

■ b. Revising paragraph (a)(2);

■ c. Removing from paragraph (b) ''component test'' and adding ''domestic content test'' in its place; and

■ d. Removing from paragraph (c) ''Subpart 25.5'' and adding ''subpart 25.5'' in its place.

The revision reads as follows:

25.101 General.

(a) * * *

(2)(i) Except for an end product that consists wholly or predominantly of iron or steel or a combination of both, the cost of domestic components must exceed 55 percent of the cost of all the components. In accordance with 41 U.S.C. 1907, this domestic content test of the Buy American statute has been waived for acquisitions of COTS items (see 12.505(a)) (but see paragraph (a)(2)(ii) of this section).

(ii) For an end product that consists wholly or predominantly of iron or steel or a combination of both, the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, must constitute less than 5 percent of the cost of all the components used in the end product. This domestic content test of the Buy American statute has not been waived for acquisitions of COTS items in this category, except for fasteners.

* * * * *

25.105 [Amended]

■ 7. Amend section 25.105 by—

■ a. Removing from paragraph (b)(1) ''6 percent'' and adding ''20 percent'' in its place; and

■ b. Removing from paragraph (b)(2) ''12 percent'' and ''Subpart 19.5'' and adding ''30 percent'' and ''subpart 19.5'' in their places, respectively.

■ 8. Amend section 25.200 by—
■ a. Removing from the end of paragraph (a)(2) ''and'';
■ b. Redesignating paragraph (a)(3) as paragraph (a)(4);
■ c. Adding a new paragraph (a)(3); and
■ d. Revising the newly redesignated paragraph (a)(4).

The addition and revision read as follows:

25.200 Scope of subpart.

(a) * * *

(3) Executive Order 13881, July 15, 2019; and

(4) Waiver of the domestic content test of the Buy American statute for acquisitions of commercially available off-the-shelf (COTS) items in accordance with 41 U.S.C. 1907, but see 25.201(b)(2)(ii).

* * * * *

■ 9. Revise section 25.201 to read as follows:

25.201 Policy.

(a) Except as provided in 25.202, use only domestic construction materials in construction contracts performed in the United States.

(b) The Buy American statute restricts the purchase of construction materials that are not domestic construction materials. For manufactured construction materials, the Buy American statute and E.O. 13881 use a two-part test to define domestic construction materials.

(1) The article must be manufactured in the United States; and

(2)(i) Except for construction material that consists wholly or predominantly of iron or steel or a combination of both, the cost of domestic components must exceed 55 percent of the cost of all the components. In accordance with 41 U.S.C. 1907, this domestic content test of the Buy American statute has been waived for acquisitions of COTS items (see 12.505(a)).

(ii) For construction material that consists wholly or predominantly of iron or steel or a combination of both, the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, must constitute less than 5 percent of the cost of all the components used in such construction material. This domestic content test of the Buy American statute has not been waived for acquisitions of COTS items in this category, except for fasteners.

25.204 [Amended]

■ 10. Amend section 25.204 in paragraph (b) by removing ''6 percent'' and adding ''20 percent'' in its place.

■ 11. Amend section 25.504–1 by—
■ a. Revising the table in paragraph (a)(1);
■ b. Removing from paragraph (a)(2) ''12 percent'' and ''$11,200'' and adding ''30 percent'' and ''$13,000'' in their places, respectively; and
■ c. Removing from paragraph (b)(2) ''12 percent'' and ''$11,424'' and adding ''30 percent'' and ''$13,260'' in their places, respectively.

The revision reads as follows:

25.504–1 Buy American statute.

(a)(1) * * *

Offer A	$16,000	Domestic end product, small business.
Offer B	15,700	Domestic end product, small business.
Offer C ...	10,000	U.S.-made end product (not domestic), small business.

* * * * *

■ 12. Amend section 25.504–2 by revising the table to read as follows:

25.504–2 WTO GPA/Caribbean Basin Trade Initiative/FTAs.

* * * * *

Offer A	$304,000	U.S.-made end product (not domestic).
Offer B	303,000	U.S.-made end product (domestic), small business.
Offer C ...	300,000	Eligible product.
Offer D ...	295,000	Noneligible product (not U.S.-made).

* * * * *

■ 13. Amend section 25.504–3 by—
■ a. Revising the entry ''Offer B'' in the table in paragraph (a);
■ b. Revising the entry ''Offer B'' in the table in paragraph (b); and
■ c. Revising entries ''Offer B'' and ''Offer C'' in the table in paragraph (c).

The revisions read as follows:

25.504–3 FTA/Israeli Trade Act.

(a) * * *

*	*	* * *
Offer B ...	$100,000	Eligible product.

* * * * *

(b) * * *

*	*	* * *
Offer B ...	$103,000	Noneligible product.

* * * * *

(c) * * *

*	*	* * *
Offer B ...	$103,000	Eligible product.
Offer C ...	100,000	Noneligible product.

* * * * *

■ 14. Amend section 25.504–4 by—
■ a. In paragraph (a)—
■ i. Revising the table;
■ ii. In STEP 1, Items 3 and 5, removing ''6 percent'' and adding ''20 percent'' in their places, respectively; and
■ iii. Revising STEP 2 and 3.
■ b. Revising paragraph (b).

The revisions read as follows:

25.504–4 Group award basis.

(a) * * *

Item	Offers		
	A	B	C
1	DO = $55,000	EL = $56,000	NEL = $50,000.
2	NEL = 13,000	EL = 10,000	EL = 13,000
3	NEL = 11,500	DO = 12,000	DO = 10,000
4	NEL = 24,000	EL = 28,000	NEL = 22,000
5	DO = 18,000	NEL = 10,000	DO = 14,000
Total	121,500	116,000	109,000

* * * * *

STEP 2: Evaluate Offer C against the tentative award pattern for Offers A and B:

Item	Offers		
	Low offer	Tentative award pattern from A and B	C
1	A	DO = $55,000	* NEL = $60,000.
2	B	EL = 10,000	EL = 13,000
3	B	DO = 12,000	DO = 10,000
4	A	NEL = 24,000	NEL = 22,000
5	B	*NEL = 12,000	DO = 14,000
Total		113,000	119,000

* Offer + 20 percent.

On a line item basis, apply a factor to any noneligible offer if the other offer for that line item is domestic.

For Item 1, apply a factor to Offer C because Offer A is domestic and the acquisition was not covered by the WTO GPA. The evaluated price of Offer C, Item 1, becomes $60,000 ($50,000 plus 20 percent). Apply a factor to Offer B, Item 5, because it is a noneligible product and Offer C is domestic. The evaluated price of Offer B is $12,000 ($10,000 plus 20 percent). Evaluate the remaining items without applying a factor.

STEP 3: The tentative unrestricted award pattern from Offers A and B is lower than the evaluated price of Offer C. Award the combination of Offers A and B. Note that if Offer C had not specified all-or-none award, award would be made on Offer C for line items 3 and 4, totaling an award of $32,000.

(b) *Example 2.*

Item	Offers		
	A	B	C
1	DO = $50,000	EL = $50,500	NEL = $50,000.
2	NEL = 10,300	NEL = 10,000	EL = 10,200
3	EL = 20,400	EL = 21,000	NEL = 20,200
4	DO = 10,500	DO = 10,300	DO = 10,400
Total	91,200	91,800	90,800

Problem: The solicitation specifies award on a group basis. Assume the Buy American statute applies and the acquisition cannot be set aside for small business concerns. All offerors are large businesses.

Analysis: (See 25.503(c))

STEP 1: Determine which of the offers are domestic (see 25.503(c)(1)):

	Domestic (percent)	Determination
A	$50,000 (Offer A1) + $10,500 (Offer A4) = $60,500 $60,500/$91,200 (Offer A Total) = 66.3%.	Domestic.
B	$10,300 (Offer B4)/$91,800 (Offer B Total) = 11.2%	Foreign.
C	$10,400 (Offer C4)/$90,800 (Offer C Total) = 11.5%	Foreign.

STEP 2: Determine whether foreign offers are eligible or noneligible offers (see 25.503(c)(2)):

	Domestic + eligible (percent)	Determination
A	N/A (Both Domestic)	Domestic.
B	$50,500 (Offer B1) + $21,000 (Offer B3) + $10,300 (Offer B4) = $81,800 $81,800/$91,800 (Offer B Total) = 89.1%.	Eligible.
C	$10,200 (Offer C2) + $10,400 (Offer C4) = $20,600 $20,600/$90,800 (Offer C Total) = 22.7%.	Noneligible.

STEP 3: Determine whether to apply an evaluation factor (see 25.503(c)(3)). The low offer (Offer C) is a foreign offer. There is no eligible offer lower than the domestic offer. Therefore, apply the factor to the low offer. Addition of the 20 percent factor (use 30 percent if Offer A is a small business) to Offer C yields an evaluated price of $108,960 ($90,800 + 20 percent). Award on Offer A (see 25.502(c)(4)(ii)). Note that, if Offer A were greater than Offer B, an evaluation factor would not be applied, and award would be on Offer C (see 25.502(c)(3)).

25.601 [Amended]

■ 15. Amend section 25.601 by removing the definition "Steel".

25.604 [Amended]

■ 16. Amend section 25.604 in paragraph (c)(2) by removing ''6 percent'' and adding ''20 percent'' in its place.

25.605 [Amended]

■ 17. Amend section 25.605 by—

■ a. Removing from paragraph (a)(2) ''6 percent'' and adding ''20 percent'' in its place; and

■ b. Removing from paragraph (a)(3) ''.06'' and adding ''.20'' in its place.

PART 52—SOLICITATION PROVISIONS AND CONTRACT CLAUSES

■ 18. Amend section 52.212–3 by—

■ a. Revising the date of the provision; and

■ b. Revising paragraphs (f)(1), (g)(1)(i), the first sentence of (g)(1)(ii), and (g)(1)(iii) introductory text.

The revisions read as follows:

52.212–3 Offeror Representations and Certifications—Commercial Items.

* * * * *

Offeror Representations and Certifications—Commercial Items (DATE)

* * * * *

(f) * * *

(1)(i) The Offeror certifies that each end product, except those listed in paragraph (f)(2) of this provision, is a domestic end product.

(ii) The Offeror shall list as foreign end products those end products manufactured in the United States that do not qualify as domestic end products.

(iii) The terms ''domestic end product,'' ''end product,'' ''foreign end product,'' and ''United States'' are defined in the clause of this solicitation entitled ''Buy American-Supplies.''

* * * * *

(g)(1) * * *

(i)(A) The Offeror certifies that each end product, except those listed in paragraph (g)(1)(ii) or (iii) of this provision, is a domestic end product.

(B) The terms ''Bahrainian, Moroccan, Omani, Panamanian, or Peruvian end product,'' ''domestic end product,'' ''end product,'' ''foreign end product,'' ''Free Trade Agreement country,'' ''Free Trade Agreement country end product,'' ''Israeli end product,'' and ''United States'' are defined in the clause of this solicitation entitled ''Buy American—Free Trade Agreements—Israeli Trade Act.''

(ii) The Offeror certifies that the following supplies are Free Trade Agreement country end products (other than Bahrainian, Moroccan, Omani, Panamanian, or Peruvian end products) or Israeli end products as defined in the clause of this solicitation entitled ''Buy American—Free Trade Agreements—Israeli Trade Act.''

* * * * *

(iii) The Offeror shall list those supplies that are foreign end products (other than those listed in paragraph (g)(1)(ii) of this provision) as defined in the clause of this solicitation entitled ''Buy American—Free Trade Agreements—Israeli Trade Act.'' The Offeror shall list as other foreign end products those end products manufactured in the United States that do not qualify as domestic end products.

* * * * *

■ 19. Amend section 52.212–5 by—

■ a. Revising the date of the clause; and

■ b. Removing from paragraphs (b)(48) and (b)(49)(i) through (iv) ''(MAY 2014)'' and adding ''(DATE)'' in their places, respectively.

The revision reads as follows:

52.212–5 Contract Terms and Conditions Required To Implement Statutes or Executive Orders—Commercial Items.

* * * * *

Contract Terms and Conditions Required To Implement Statutes or Executive Orders—Commercial Items (DATE)

* * * * *

■ 20. Amend section 52.213–4 by—

■ a. Revising the date of the clause; and

■ b. Removing from paragraph (b)(1)(xvii) introductory text ''(MAY 2014)'' and adding ''(DATE)'' in its place.

The revision reads as follows:

52.213–4 Terms and Conditions—Simplified Acquisitions (Other Than Commercial Items).

* * * * *

Terms and Conditions—Simplified Acquisitions (Other Than Commercial Items) (DATE)

* * * * *

■ 21. Amend section 52.225–1 by—

■ a. Revising the date of the clause;

■ b. In paragraph (a):

■ i. Revising the definition ''Domestic end product''; and

■ ii. Adding in alphabetical order the definitions ''Fastener'' and ''Steel''; and

■ c. Revising paragraph (b).

The revisions and additions read as follows:

52.225–1 Buy American—Supplies.

* * * * *

Buy American—Supplies (DATE)

(a) * * *

Domestic end product means—

(1) For an end product that does not consist wholly or predominantly of iron or steel or a combination of both—

(i) An unmanufactured end product mined or produced in the United States;

(ii) An end product manufactured in the United States, if—

(A) The cost of its components mined, produced, or manufactured in the United States exceeds 55 percent of the cost of all its components. Components of foreign origin of the same class or kind as those that the agency determines are not mined, produced, or manufactured in sufficient and reasonably available commercial quantities of a satisfactory quality are treated as domestic. Components of unknown origin are treated as foreign. Scrap generated, collected, and prepared for processing in the United States is considered domestic; or

(B) The end product is a COTS item; or

(2) For an end product that consists wholly or predominantly of iron or steel or a combination of both, an end product manufactured in the United States, if the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, constitutes less than 5 percent of the cost of all the components used in the end product (produced in the United States means that all manufacturing processes of the iron or steel must take place in the United States, except metallurgical processes involving refinement of steel additives).

* * * * *

Fastener means a hardware device that mechanically joins or affixes two or more objects together. Examples of fasteners are nuts, bolts, pins, rivets, nails, clips, and screws.

* * * * *

Steel means an alloy that includes at least 50 percent iron, between .02 and 2 percent carbon, and may include other elements.

* * * * *

(b) 41 U.S.C. chapter 83, Buy American, provides a preference for domestic end products for supplies acquired for use in the United States. In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for an end product that is a COTS item (see 12.505(a)(1)), except that for an end product that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the end product, excluding fasteners.

* * * * *

■ 22. Amend section 52.225–2 by revising the date of the provision and paragraph (a) to read as follows:

52.225–2 Buy American Certificate.

* * * * *

Buy American Certificate (DATE)

(a)(1) The Offeror certifies that each end product, except those listed in paragraph (b) of this provision, is a domestic end product.

(2) The Offeror shall list as foreign end products those end products manufactured in the United States that do not qualify as domestic end products.

(3) The terms ‘‘domestic end product,’’ ‘‘end product,’’ and ‘‘foreign end product’’ are defined in the clause of this solicitation entitled ‘‘Buy American—Supplies.’’

* * * * *

■ 23. Amend section 52.225–3 by—
■ a. Revising the date of the clause;
■ b. In paragraph (a):
■ i. Revising the definition ‘‘Domestic end product’’; and
■ ii. Adding in alphabetical order the definitions ‘‘Fastener’’ and ‘‘Steel’’;
■ c. Revising the second sentence of paragraph (c);
■ d. Revising the date in the introductory text and the second sentence of paragraph (c) of Alternate I;
■ e. Revising the date in the introductory text and the second sentence of paragraph (c) of Alternate II; and
■ f. Revising the date in the introductory text and the second sentence of paragraph (c) of Alternate III.

The revisions and additions read as follows:

52.225–3 Buy American—Free Trade Agreements—Israeli Trade Act.

* * * * *

Buy American—Free Trade Agreements—Israeli Trade Act (DATE)

(a) * * *

Domestic end product means—

(1) For an end product that does not consist wholly or predominantly of iron or steel or a combination of both—

(i) An unmanufactured end product mined or produced in the United States;

(ii) An end product manufactured in the United States, if—

(A) The cost of its components mined, produced, or manufactured in the United States exceeds 55 percent of the cost of all its components. Components of foreign origin of the same class or kind as those that the agency determines are not mined, produced, or manufactured in sufficient and reasonably available commercial quantities of a satisfactory quality are treated as domestic. Components of unknown origin are treated as foreign. Scrap generated, collected, and prepared for processing in the United States is considered domestic; or

(B) The end product is a COTS item; or

(2) For an end product that consists wholly or predominantly of iron or steel or a combination of both, an end product manufactured in the United States, if the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, constitutes less than 5 percent of the cost of all the components used in the end product (produced in the United States means that all manufacturing processes of the iron or steel must take place in the United States, except metallurgical processes involving refinement of steel additives).

* * * * *

Fastener means a hardware device that mechanically joins or affixes two or more objects together. Examples of fasteners are nuts, bolts, pins, rivets, nails, clips, and screws.

* * * * *

Steel means an alloy that includes at least 50 percent iron, between .02 and 2 percent carbon, and may include other elements.

* * * * *

(c) * * * In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for an end product that is a COTS item (see 12.505(a)(1)), except that for an end product that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the end product, excluding fasteners. * * *

Alternate I (DATE) * * *

(c) * * * In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for an end product that is a COTS item (see 12.505(a)(1)), except that for an end product that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the end product, excluding fasteners. * * *

Alternate II (DATE) * * *

(c) * * * In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for an end product that is a COTS item (see 12.505(a)(1)), except that for an end product that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the end product, excluding fasteners. * * *

Alternate III (DATE) * * *

(c) * * * In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for an end product that is a COTS item (see 12.505(a)(1)), except that for an end product that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the end product, excluding fasteners. * * *

■ 24. Amend section 52.225–4 by—
■ a. Revising the date of the provision;
■ b. Revising paragraph (a);
■ c. In paragraph (b) introductory text removing ‘‘offeror’’ and adding ‘‘Offeror’’ in its place;
■ d. Revising the first and second sentences of paragraph (c);
■ e. In Alternate I by—
■ i. Revising the date of the Alternate; and
■ ii. Removing from paragraph (b) introductory text ‘‘offeror’’ and adding ‘‘Offeror’’ in its place;
■ f. In Alternate II by—
■ i. Revising the date of the Alternate; and
■ ii. Removing from paragraph (b) introductory text ‘‘offeror’’ and adding ‘‘Offeror’’ in its place; and
■ g. In Alternate III by—
■ i. Revising the date of the Alternate; and
■ ii. Removing from paragraph (b) introductory text ‘‘offeror’’ and adding ‘‘Offeror’’ in its place.

The revisions read as follows:

52.225–4 Buy American-Free Trade Agreements-Israeli Trade Act Certificate.

* * * * *

Buy American-Free Trade Agreements-Israeli Trade Act Certificate (DATE)

(a)(1) The Offeror certifies that each end product, except those listed in paragraph (b) or (c) of this provision, is a domestic end product.

(2) The terms ‘‘Bahrainian, Moroccan, Omani, Panamanian, or Peruvian end product,’’ ‘‘domestic end product,’’ ‘‘end product,’’ ‘‘foreign end product,’’ ‘‘Free Trade Agreement country,’’ ‘‘Free Trade Agreement country end product,’’ ‘‘Israeli end product,’’ and ‘‘United States’’ are defined in the clause of this solicitation entitled ‘‘Buy American-Free Trade Agreements–Israeli Trade Act.’’

* * * * *

(c) The Offeror shall list those supplies that are foreign end products (other than those listed in paragraph (b) of this provision) as defined in the clause of this solicitation entitled ‘‘Buy American—Free Trade Agreements—Israeli Trade Act.’’ The Offeror shall list as other foreign end products those end products manufactured in the United States that do not qualify as domestic end products.

* * * * *

Alternate I (DATE) * * *

Alternate II (DATE) * * *

Alternate III (DATE) * * *

■ 25. Amend section 52.225–9 by—
■ a. Revising the date of the clause;
■ b. In paragraph (a):
■ i. Revising the definition ‘‘Domestic construction material’’; and
■ ii. Adding in alphabetical order the definitions ‘‘Fastener’’ and ‘‘Steel’’;
■ c. Revising paragraph (b)(1); and
■ d. Removing from paragraph (b)(3)(i) ‘‘6 percent’’ and adding ‘‘20 percent’’ in its place.

The revisions and additions read as follows:

52.225–9 Buy American—Construction Materials.

* * * * *

Buy American—Construction Materials (DATE)

(a) * * *

Domestic construction material means—

(1) For construction material that does not consist wholly or predominantly of iron or steel or a combination of both—

(i) An unmanufactured construction material mined or produced in the United States; or

(ii) A construction material manufactured in the United States, if—

(A) The cost of its components mined, produced, or manufactured in the United States exceeds 55 percent of the cost of all its components. Components of foreign origin of the same class or kind for which nonavailability determinations have been made are treated as domestic. Components of unknown origin are treated as foreign; or

(B) The construction material is a COTS item.

(2) For construction material that consists wholly or predominantly of iron or steel or a combination of both, a construction material manufactured in the United States if the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, constitutes less than 5 percent of the cost of all components used in such construction material (produced in the United States means that all manufacturing processes of the iron or steel must take place in the United States, except metallurgical processes involving refinement of steel additives).

Fastener means a hardware device that mechanically joins or affixes two or more objects together. Examples of fasteners are nuts, bolts, pins, rivets, nails, clips, and screws.

* * * * *

Steel means an alloy that includes at least 50 percent iron, between .02 and 2 percent carbon, and may include other elements.

* * * * *

(b) * * * (1) This clause implements 41 U.S.C. chapter 83, Buy American, by providing a preference for domestic construction material. In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for construction material that is a COTS item, except that for construction material that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the construction materials, excluding fasteners. (See FAR 12.505(a)(2)). The Contractor shall use only domestic construction material in performing this contract, except as provided in paragraphs (b)(2) and (b)(3) of this clause.

* * * * *

■ 26. Amend section 52.225–11 by—
■ a. Revising the date of the clause;
■ b. In paragraph (a):
■ i. Revising the definition ''Domestic construction material''; and
■ ii. Adding in alphabetical order the definitions ''Fastener'' and ''Steel'';
■ c. Revising paragraph (b)(1);
■ d. Removing from paragraph (b)(4)(i) ''6 percent'' and adding ''20 percent'' in its place; and
■ e. In Alternate I—
■ i. Revising the date of the Alternate; and
■ ii. Revising paragraph (b)(1).

The revisions and additions read as follows:

52.225–11 Buy American—Construction Materials Under Trade Agreements.

* * * * *

Buy American—Construction Materials Under Trade Agreements (DATE)

(a) * * *

Domestic construction material means—

(1) For construction material that does not consist wholly or predominantly of iron or steel or a combination of both—

(i) An unmanufactured construction material mined or produced in the United States; or

(ii) A construction material manufactured in the United States, if—

(A) The cost of its components mined, produced, or manufactured in the United States exceeds 55 percent of the cost of all its components. Components of foreign origin of the same class or kind for which nonavailability determinations have been made are treated as domestic. Components of unknown origin are treated as foreign; or

(B) The construction material is a COTS item;

(2) For construction material that consists wholly or predominantly of iron or steel or a combination of both, a construction material manufactured in the United States if the cost of iron and steel not produced in the United States (excluding fasteners) as estimated in good faith by the contractor, constitutes less than 5 percent of the cost of all components used in such construction material (produced in the United States means that all manufacturing processes of the iron or steel must take place in the United States, except metallurgical processes involving refinement of steel additives).

Fastener means a hardware device that mechanically joins or affixes two or more objects together. Examples of fasteners are nuts, bolts, pins, rivets, nails, clips, and screws.

* * * * *

Steel means an alloy that includes at least 50 percent iron, between .02 and 2 percent carbon, and may include other elements.

* * * * *

(b) * * * (1) This clause implements 41 U.S.C. chapter 83, Buy American, by providing a preference for domestic construction material. In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for construction material that is a COTS item, except that for construction material that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the construction material, excluding fasteners. (See FAR 12.505(a)(2)). In addition, the Contracting Officer has determined that the WTO GPA and Free Trade Agreements (FTAs) apply to this acquisition. Therefore, the Buy American restrictions are waived for designated country construction materials.

* * * * *

Alternate I (DATE) * * *

(b) * * * (1) This clause implements 41 U.S.C. chapter 83, Buy American, by providing a preference for domestic construction material. In accordance with 41 U.S.C. 1907, the domestic content test of the Buy American statute is waived for construction material that is a COTS item, except that for construction material that consists wholly or predominantly of iron or steel or a combination of both, the domestic content test is applied only to the iron and steel content of the construction material, excluding fasteners. (See FAR 12.505(a)(2)). In addition, the Contracting Officer has determined that the WTO GPA and all the Free Trade Agreements except the Bahrain FTA, NAFTA, and the Oman FTA apply to this acquisition. Therefore, the Buy American statute restrictions are waived for designated country construction materials other than Bahrainian, Mexican, or Omani construction materials.

* * * * *

■ 27. Amend section 52.225–21 by—
■ a. Revising the date of the clause;
■ b. Removing from paragraph (b)(4)(i)(B) ''6 percent'' and adding ''20 percent'' in its place;
■ c. Removing from paragraph (c) heading ''*Section*'' and adding ''*section*'' in its place; and
■ d. In paragraph (d):
■ i. Removing from the first undesignated paragraph following the table ''reponse'' and adding ''response'' in its place; and
■ ii. Removing from the second undesignated paragraph following the table ''**Include*'' and adding ''*[*Include*'' in its place.

The revision reads as follows:

52.225–21 Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials.

* * * * *

Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials (DATE)

* * * * *

■ 28. Amend section 52.225–22 by—
■ a. Revising the date of the provision;
■ b. Removing from paragraph (b) ''offeror'' and adding ''Offeror'' in its place wherever it appears;
■ c. Removing from paragraph (c)(1)(ii) ''6 percent'' and adding ''20 percent'' in its place;
■ d. Removing from paragraph (c)(3) ''offeror'' and adding ''Offeror'' in its place; and
■ e. Removing from paragraphs (d)(1), (2), and (3) introductory text ''offeror'' and adding ''Offeror'' in their places, respectively.

The revision reads as follows:

52.225–22 Notice of Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials.

* * * * *

Notice of Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials (DATE)

* * * * *

■ 29. Amend section 52.225–23 by—

■ a. Revising the date of the clause; and

■ b. Removing from paragraph (b)(4)(i)(B) ''6 percent'' and adding ''20 percent'' in its place.

The revision reads as follows:

52.225–23 Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials Under Trade Agreements.

* * * * *

Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials Under Trade Agreements (DATE)

* * * * *

■ 30. Amend section 52.225–24 by—

■ a. Revising the date of the provision;

■ b. Removing from paragraph (b) ''offeror'' and adding ''Offeror'' in its place wherever it appears;

■ c. Removing from paragraph (c)(1)(ii) ''6 percent'' and adding ''20 percent'' in its place;

■ d. Removing from paragraph (c)(3) ''offeror'' and adding ''Offeror'' in its place; and

■ e. Removing from paragraphs (d)(1), (2), and (3) introductory text ''offeror'' and adding ''Offeror'' in their places, respectively.

The revision reads as follows:

52.225–24 Notice of Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials Under Trade Agreements.

* * * * *

Notice of Required Use of American Iron, Steel, and Manufactured Goods—Buy American Statute—Construction Materials Under Trade Agreements (DATE)

* * * * *

[FR Doc. 2020–20116 Filed 9–11–20; 8:45 am]

BILLING CODE 6820–EP–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

50 CFR Part 600

[RTID 0648–XA356]

Magnuson-Stevens Act Provisions; General Provisions for Domestic Fisheries; Pacific Coast Groundfish Fishery; Application for an Exempted Fishing Permit

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notification; request for comments.

SUMMARY: NMFS announces the receipt of an exempted fishing permit application titled, ''*Year-round Coastwide Midwater Rockfish EFP: Monitoring and Minimizing Salmon Bycatch When Targeting Rockfish in the Shorebased IFQ Fishery, 2021–2022.*'' The application, submitted by the West Coast Seafood Processors Association, Environmental Defense Fund, Oregon Trawl Commission, and Midwater Trawlers Cooperative, requests a permit to test whether removing certain gear, time, and area restrictions for vessels fishing under the West Coast Groundfish Trawl Rationalization Program's Shorebased Individual Fishing Quota Program may impact the nature and extent of bycatch of prohibited species (*e.g.,* Chinook salmon). This exempted fishing permit would allow participating groundfish bottom and midwater trawl vessels more flexibility than allowed in current regulations to target pelagic rockfish species, such as widow, chilipepper, and yellowtail rockfish. Regulations under the Magnuson-Stevens Fishery Conservation and Management Act require publication of this notification to provide interested parties the opportunity to comment on applications for proposed exempted fishing permits.

DATES: Comments must be received no later than 5 p.m., local time on September 29, 2020.

ADDRESSES: You may submit comments on this document, identified by NOAA–NMFS–2020–0097, by the following method:

- *Electronic Submissions:* Submit all electronic public comments via the Federal e-Rulemaking Portal. Go to *www.regulations.gov/#!docketDetail;D=NOAA-NMFS-2020-0097,* click the ''Comment Now!'' icon, complete the required fields, and enter or attach your comments. The EFP application will be available under ''Supporting and Related Materials'' through the same link.

Instructions: Comments sent by any other method, to any other address or individual, or received after the end of the comment period, may not be considered by NMFS. All comments received are a part of the public record and would generally be posted for public viewing on *www.regulations.gov* without change. All personal identifying information (*e.g.,* name, address, etc.), confidential business information, or otherwise sensitive information submitted voluntarily by the sender would be publicly accessible. NMFS would accept anonymous comments (enter ''N/A'' in the required fields if you wish to remain anonymous). Attachments to electronic comments would be accepted in Microsoft Word, Excel, or Adobe PDF file formats only.

FOR FURTHER INFORMATION CONTACT: Lynn Massey, West Coast Region, NMFS, at (562) 436–2462, *lynn.massey@noaa.gov.*

SUPPLEMENTARY INFORMATION: This action is authorized by the Pacific Coast Groundfish Fishery Management Plan (FMP) and regulations at 50 CFR 600.745, which allow NMFS Regional Administrators to authorize exempted fishing permits (EFPs) to test fishing activities that would otherwise be prohibited.

At the June 2020 Pacific Fishery Management Council (Council) meeting, the Council voted to recommend that NMFS approve an EFP application titled, ''*Year-round Coastwide Midwater Rockfish EFP: Monitoring and Minimizing Salmon Bycatch When Targeting Rockfish in the Shorebased IFQ Fishery, 2021–2022*'' (herein referred to as the ''2021 Trawl Gear EFP'') for the 2021 fishing year, and made the preliminary decision to recommend continuing the EFP project in 2022. The applicants (*i.e.,* the West Coast Seafood Processors Association, Environmental Defense Fund, Oregon Trawl Commission, and Midwater Trawlers Cooperative) submitted the application as a renewal request to continue EFP research conducted since 2017; the multi-year EFP project is collectively referred to as the ''Trawl Gear EFP.'' The Trawl Gear EFP project allows up to 60 vessels participating in the West Coast Groundfish Trawl Rationalization Program's Limited Entry Shorebased Individual Fishing Quota (IFQ) Program to test whether removing certain gear, time, and area restrictions may impact the nature and extent of bycatch of protected and prohibited species (*i.e.,* Chinook salmon, coho, eulachon, and green sturgeon). Since 2017, NMFS has annually modified the suite of exemptions allowed under the Trawl Gear EFP project as certain groundfish regulations are lifted or revised. For a history of the authorized exemptions, see 81 FR 96437 (December 30, 2016) for the 2017 EFP, 82 FR 52882 (November 15, 2017) for the 2018 EFP, 83 FR 61603 (November 30, 2018) for the 2019 EFP, and 84 FR 56246 (October 22, 2019) for the 2020 EFP. Exemptions originally proposed by the applicants and published in the **Federal Register** notice for the 2020 Trawl Gear EFP were later modified to reflect regulatory changes to groundfish closed areas implemented via Amendment 28 to the Pacific Coast Groundfish FMP (*See* 84 FR 63966, November 19, 2019). The modified 2020 Trawl Gear EFP exemptions are consistent with the exemptions requested by the applicants for the 2021 and 2022 Trawl Gear EFPs (see below list).

For the 2021 Trawl Gear EFP project, the application requests exemptions from the following limited entry trawl fisheries regulations:

- For vessels fishing with *bottom trawl* groundfish gear:
  - The requirement to use selective flatfish trawl gear, and the prohibition on using small footrope gear other than selective flatfish trawl gear between 42° and 40°10′ North latitude (N) and shoreward of the boundary line approximating the 100 fathom (fm) depth contour (*See* § 660.130(c)(2)(i) and (c)(2)(ii)); and
  - The requirement that selective flatfish trawl must be a two-seamed net with no more than two riblines, excluding the codend (*See* § 660.130(b)(1)(ii)(A)).
- For vessels fishing with *midwater trawl* groundfish gear:
  - The prohibition on fishing outside the primary season dates for the Pacific whiting IFQ fishery (See § 660.112(b)(x) and § 660.130(c)(3));
  - The prohibition on fishing south of 40°10′ N lat. shoreward of the boundary line approximating the 150 fm depth contour (*See* § 660.130(c)(3)(ii) and (c)(4)(ii)(B)).
- For vessels fishing with *either midwater or bottom trawl* groundfish gear:
  - The prohibition on retaining certain prohibited species (*See* § 660.12 (a)(1)); and
  - The requirement to discard certain prohibited species at sea (*See* § 660.140 (g)(1)).

If NMFS approves this EFP, vessels fishing on an EFP trip with limited entry bottom trawl gear would be permitted to use any small footrope gear that meets the definition in regulations at § 660.11 between 42° N lat. and 40°10′ N lat and shoreward of the 100 fm depth contour. Vessels fishing on an EFP trip with limited entry bottom trawl gear would also be permitted to use both two- and four-seam selective flatfish trawl nets with two- or four-riblines, excluding the codend. Vessels fishing on an EFP trip with limited entry midwater trawl gear would be permitted to fish south of 40°10′ N lat. shoreward of the 150 fm depth contour. Additionally, vessels fishing on an EFP trip with limited entry midwater trawl gear would not be constrained to the Pacific whiting primary season dates in existing groundfish regulations. Participating vessels would be required to carry observers or use a NMFS-approved electronic monitoring system on 100 percent of trips, as is currently required in the IFQ program. Participating vessels would also be required to retain all salmon (excluding salmon already sampled by NMFS' West Coast Groundfish Observer Program) until offloading.

A goal of this EFP project is to collect information on the effects of lifting the restrictions described above on bycatch, including bycatch of Endangered Species Act (ESA)-listed salmon, eulachon, and green sturgeon. Previous analyses suggest that bycatch rates of these ESA-listed species could increase as a result of the changes in gear configurations from the Trawl Gear EFP. However, because a targeted fishery for chilipepper, widow, and yellowtail rockfish has not existed in more than a decade, and because the current groundfish trawl fishery has changed considerably in recent years, available data may have limited utility for predicting current impacts to protected and prohibited species in fisheries conducted with the exemptions that would be allowed under this EFP application being considered. NMFS staff worked with the applicants to inform their development of this EFP application, advising on what might increase the ability of fishery participants to target pelagic rockfish species while also minimizing bycatch to the extent practicable and ensuring adequate bycatch information can be collected. To address potential increased protected and prohibited species encounters, the Council recommended that EFP applicants adhere to area-based Chinook salmon bycatch limits for midwater trawl and bottom trawl EFP vessels in 2021 and 2022. Under this proposal, if Chinook salmon catch on EFP trips for either gear type reaches the applicable bycatch limit, NMFS would revoke the EFP for that gear type for the remainder of the year. If this EFP is approved, NMFS would set a bycatch limit of 1,000 Chinook salmon north of 42° N lat. and 100 Chinook salmon south of 42° N lat. for vessels declared into the EFP, regardless of gear type. If either of these bycatch limits are reached, NMFS would revoke the EFP for both gear types in the respective management area (*i.e.,* north or south of 42° N lat.).

The application includes a requirement to retain and land salmon bycatch on all EFP trips, consistent with current requirements for vessels participating in the shoreside Pacific whiting fishery. The intent of this provision is to provide a complete census of salmon bycatch for each EFP trip and maximize the amount of biological and genetic salmon samples. In the event that more salmon are landed than what the onboard observer can sample, the vessel would notify their respective state fish and wildlife agency upon returning to port to give them the opportunity to collect and sample the excess salmon bycatch.

The EFP applicants have not proposed a specific list of participating vessels, but consistent with previous years, are proposing that NMFS publish a public notice to gauge interest from limited entry groundfish midwater and bottom trawl vessels. Depending on the amount of interest and where vessels may be fishing, NMFS may need to limit participation by time and area to mitigate potential impacts.

Information collected under the EFP would be used to support analysis for potential new gear regulations and modifications to existing gear regulations. Because many of the current gear regulations have been in place for more than ten years, it is difficult for NMFS, the Council, and industry to predict the impacts of removing these regulations. In the past 10 years, the industry has changed significantly. Reduction in capacity, innovations in gear technologies, and changes in management have all contributed to these changes. The information collected through the fishing under this EFP would help demonstrate what potential impacts, if any, today's fleet may have if some of the current gear, area, and time regulations are modified from what is currently in regulation. NMFS has already used data from the prior years of the EFP project to modify regulations that were no longer necessary due to changes in the groundfish fishery and the improved status of several overfished groundfish stocks. For example, data from the 2017 and 2018 EFPs helped modify regulations that restricted the use and configuration of trawl gear via a December 3, 2018 final rule (*See* 83 FR 62269).

NMFS is proposing to approve the 2021 Trawl Gear EFP, and preliminarily approve the 2022 Trawl Gear EFP, covering all the exemptions stated above, following the conclusion of the public comment period and review of public comment. NMFS would not issue another **Federal Register** notice soliciting public comment on renewing the Trawl Gear EFP for 2022 unless: (1) The applicants modify and resubmit their application to NMFS; (2) changes to relevant trawl fisheries regulations warrant a revised set of exemptions authorized under the EFP project; or (3) NMFS' understanding of the current biological and economic impacts from EFP fishing activities substantially changes. Pending approval, NMFS would issue the permits for the EFP project to the vessel owner or designated representative as the ''EFP holder.'' NMFS intends to use an adaptive management approach in which NMFS may revise requirements and protocols to improve the program without issuing another **Federal Register** notice, provided that the modifications fall within the scope of the original EFP. In addition, the applicants may request minor modifications and extensions to the EFP throughout the course of research. NMFS may grant EFP modifications and extensions without further public notice if the changes are essential to facilitate completing the proposed research and result in only a minimal change in the scope or impacts of the initially approved EFP request.

NMFS analyzed the potential effects of implementing the 2018 Trawl Gear EFP in an environmental assessment (EA), dated December 2017 (Available at: *http://www.westcoast.fisheries.noaa.gov*). In that EA, NMFS stated that it anticipated issuing additional, similar, one-year EFPs that would cover a portion or all of the components discussed in the EA. Those EFPs would be supported by the analyses in the EA, as long as there were not substantial changes to the affected environment (*e.g.,* status of the stock), components of the EFP (*i.e.,* gear, area, and time restrictions), or unanticipated effects on the environment from permitting fishing activities that were not discussed in the EA's analysis. Since the 2021 and 2022 Trawl Gear EFPs meet those criteria, NMFS does not anticipate any environmental impacts from the 2021–2022 Trawl Gear EFP beyond those analyzed in the EA for the 2018 Trawl Gear and future similar EFPs. NMFS welcomes public comment on the NEPA coverage for this EFP.

After publication of this document in the **Federal Register**, NMFS may approve and issue permits for the EFP project after the close of the public comment period. NMFS will consider comments submitted in deciding whether to approve the application as requested. NMFS may approve the application in its entirety or may make any alterations needed to achieve the goals of the EFP.

Authority: 16 U.S.C. 1801 *et seq.,* 16 U.S.C. 773 *et seq.,* and 16 U.S.C. 7001 *et seq.*

Dated: August 25, 2020.

Jennifer M. Wallace,

Acting Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–19060 Filed 9–11–20; 8:45 am]

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Notices

Federal Register

Vol. 85, No. 178

Monday, September 14, 2020

DEPARTMENT OF AGRICULTURE

Farm Service Agency

Commodity Credit Corporation

[Docket ID CCC–2020–0007]

Notice of Funds Availability (NOFA); Seafood Trade Relief Program (STRP)

AGENCY: Commodity Credit Corporation, Farm Service Agency, USDA.

ACTION: Notice.

SUMMARY: The Seafood Trade Relief Program (STRP) provides payments to eligible commercial fishermen of seafood commodities that have been impacted by trade actions of foreign governments resulting in the loss of exports. This document announces the availability of STRP funds for eligible active commercial fishermen as specified in this document, consistent with the Presidential Memorandum issued on June 24, 2020, ''Protecting the United States Lobster Industry.'' The Farm Service Agency (FSA) administers STRP on behalf of the Commodity Credit Corporation (CCC). Payments are for the purpose of expanding or aiding in the expansion of domestic markets for U.S. caught and sold seafood.

DATES: *Application period:* September 14, 2020, through December 14, 2020.

Comment Date: We will consider comments on the Paperwork Reduction Act that we receive by: November 13, 2020.

ADDRESSES: We invite you to submit comments on the information collection requirements for STRP. You may submit comments by any of the following methods, although FSA and CCC prefer that you submit comments electronically through the Federal eRulemaking Portal:

- *Federal eRulemaking Portal:* Go to *http://www.regulations.gov* and search for Docket ID CCC–2020–0007. Follow the online instructions for submitting comments.
- *Mail:* William L. Beam, Deputy Administrator, Farm Programs, Farm Service Agency, USDA, 1400 Independence Ave. SW, Washington, DC 20250. In your comment, specify the docket ID CCC–2019–0007.

All comments received, including those received by mail, will be posted without change and publicly available on *http://www.regulations.gov.*

FOR FURTHER INFORMATION CONTACT: William L. Beam, Deputy Administrator for Farm Programs, telephone: (202) 720–3175.

SUPPLEMENTARY INFORMATION:

Background

The Presidential Memorandum issued on June 24, 2020, ''Protecting the United States Lobster Industry,'' (*https://www.whitehouse.gov/presidential-actions/memorandum-protecting-united-states-lobster-industry/*) directs USDA to consider taking appropriate action, as permitted by law, to provide assistance to eligible U.S. commercial fishermen with seafood production that have been impacted by trade actions of foreign governments resulting in the loss of exports. USDA, in consultation with the Department of Commerce, determined that assistance was appropriate and will be made available under section 5(e) of the CCC Charter Act (15 U.S.C. 714c). This section authorizes CCC to act to increase the domestic consumption of agricultural commodities by expanding or aiding in the expansion of domestic markets or by developing or aiding in the development of new and additional markets, marketing facilities, and uses for such commodities. FSA administers STRP on behalf of CCC.

Definitions

For STRP, the following definitions apply. These definitions of ''commercial fishing'' and ''exclusive economic zone (EEZ)'' are consistent with the definitions in the regulations of the Magnuson Stevens Fishery Conservation And Management Act, National Oceanic And Atmospheric Administration, Department Of Commerce (see 50 CFR 600.10, 622.2, and 635.2).

Commercial fishing means fishing that is intended to, or results in, the barter, trade, transfer, or sale of fish, but does not include aquaculture with the exception of geoducks and salmon.

Exclusive economic zone (EEZ) means the zone established by Presidential Proclamation 5030, 3 CFR part 22, dated March 10, 1983, and is that area adjacent to the United States that, except where modified to accommodate international boundaries, encompasses all waters from the seaward boundary of each of the coastal states to a line on which each point is 200 nautical miles (370.40 km) from the baseline from which the territorial sea of the United States is measured.

Eligibility and Payment Limits for STRP

This document announces the availability of STRP payments for commercial fishermen with seafood production reported as U.S. harvested in calendar year 2019. U.S. caught and sold seafood includes those fish or shellfish caught by U.S. vessels in Canadian waters covered by the Treaty Between the Governments of Canada and the United States on Pacific Albacore Tuna Vessels and Port Privileges.

Eligible STRP production only includes marine species that are harvested by commercial fisherman who hold a valid federal or state license or permit to catch seafood, and such marine species are brought to shore and sold or transferred to another party that must be a legally permitted or licensed seafood dealer or processed at sea and sold by the same legally permitted entity that harvested or processed the product. Any seafood that is not sold to a permitted dealer or by a permitted dealer if the catch is processed at sea is ineligible for payment. Only those species and types of seafood listed in the table in this document are eligible for STRP payments. Geoducks and salmon are the only aquaculture production with estimated trade damages of more than $5 million as required by STRP.

No person or legal entity, excluding a joint venture or general partnership, as determined by the regulations in 7 CFR part 1400 may receive, directly or indirectly, more than $250,000 in payments made pursuant to this NOFA.

In general, STRP applicants with an average adjusted gross income (AGI) of $900,000 or more are not eligible to receive an STRP payment. Specifically, the $900,000 average AGI limitation provisions in 7 CFR part 1400 relating to limits on payments for persons or legal entities, excluding joint ventures and general partnerships, apply to each commercial fisherman as an applicant for STRP. The average AGI will be calculated for a person or legal entity based on the 3 complete tax years that precede the year for which the payment is made (for 2020 the tax years are 2016, 2017, and 2018). However, if the average AGI of a person or legal entity is greater than $900,000, the person or entity is not eligible to receive a STRP payment, unless at least 75 percent of the adjusted gross income of the person or entity is derived from farming, ranching, forestry, seafood production, or related activities.

State and local governments are not eligible.

In general, foreign persons are not eligible for STRP payments. Specifically, the foreign persons rules in 7 CFR part 1400, subpart E apply in determining eligibility for payments made according to this NOFA and for purposes of application of this subpart under this NOFA, production of seafood will be treated as production on a farm.

When applying, the U.S. commercial fisherman applicant will certify to FSA, on form CCC–916, the ownership share in pounds of the commercially produced seafood as reported to Federal and State fisheries, this includes harvested production in Territories of the U.S.. In order to be eligible for STRP, U.S. commercial fishermen operations must be in business at the time of application. Those commercial fishermen operations that are not in business at the time of application are therefore ineligible for STRP. A person or legal entity will be ineligible for STRP, if for a portion or all of the 2020 calendar year, such person or legal entity either:

- Does not have an ownership interest in the production; or
- Does not have a Federal or State permit for commercial fishing to harvest seafood.

Applicants must comply with the provisions of:

- This NOFA; and
- Form CCC–916 (and any required production evidence, if requested by FSA).

Application Process

Each eligible commercial fisherman applies for STRP participation once by completing a ''2020 Seafood Trade Relief Program (STRP) Application'' (form CCC–916), which is available on *www.farmers.gov* and in FSA county offices. Each applicant must submit a complete form CCC–916 either in person, by mail, email, or facsimile to an FSA county office. Applicants may submit form CCC–916 in any county office nationwide. If a producer who applies must submit additional documentation for eligibility, such as certifications of compliance with payment limitation on form CCC–902 and adjusted gross income provisions on form CCC–941, or proof of a commercial license, those additional documents and forms must be submitted no later than 60 days from the date the producer signs the application.

No STRP payment will be issued until an applicant certifies, as applicable, the quantity of 2019 commercial production reported in pounds to Federal or State fisheries. The applicant must certify to the total commercial production by the application period deadline as specified in this document.

Trade Disruptions

There remain retaliatory tariffs by China on American seafood exports, which continue to disrupt seafood markets. The extent of those disruptions can be measured by estimating the extent to which seafood trade can reasonably be expected to be impacted by those retaliatory tariffs relative to pre-tariff trade.

The STRP rates were calculated using USDA's assessment of the expected trade damage using partial equilibrium trade modeling. The model for each commodity is based on economic theory and each employ modeling frameworks and parameters widely recognized and utilized in both the academic and trade policy communities. Based on the increased tariff, the models simulate the expected reduction in U.S. exports to the retaliatory partner market, holding other factors constant. Trade damages are calculated as the difference in trade with the tariff and the baseline (without the tariff).

The expected trade impacts depend on several factors, including the tariff levels, the amount of production affected by the trade disruption, the sensitivity of the retaliating country's consumers to higher prices due to the tariffs, and the availability of substitutes for U.S. products. The trade model factors all of these variables and the damage results provide an estimate for the adjustment costs due to the trade disruption. The rates are determined by allocating the adjustment costs over the affected supply to obtain a per-unit basis.

The methodology is similar to the approach USDA employed to estimate the trade damages for U.S. commodities affected by retaliatory tariffs to establish commodity payment rates for the Market Facilitation Program (MFP) and purchase targets for the Food Purchase and Distribution Program (FPDP). USDA provided a detailed accounting of how those gross damage estimates were calculated which may be found here:

2018 MFP and FPDP: https://www.usda.gov/sites/default/files/documents/USDA_Trade_Methodology_Report_2018.pdf.

2019 MFP and FPDP: https://www.usda.gov/sites/default/files/documents/USDA_Trade_Methodology_Report_2019.pdf.

Payment Rates and Payment Calculations

Data on impacted seafood tariffs [1] and global trade flows of seafood products in 2017 [2] was used to estimate gross trade damages. Average domestic landings between 2017 and 2019 were used to determine payment rates per pound of eligible commodity.[3] Commodities with estimated trade damages of less than $5 million were not considered.

Species group [1]	Value of China's imports of U.S. seafood products (2017) [2] (in million $)	Trade damage (model estimates) (in million $)	U.S. domestic landings (2017–2019) [3] (in million lbs)
Salmon	$319	$135	840
Sole, Flounder, and Turbot	185	78	525
Pacific Cod	177	75	545
Lobsters	167	71	142

[1] The average size of China's retaliatory tariff on U.S. seafood products is 30%.

[2] Trade Data Monitor.

[3] NOAA fisheries.

Species group [1]	Value of China's imports of U.S. seafood products (2017) [2] (in million $)	Trade damage (model estimates) (in million $)	U.S. domestic landings (2017–2019) [3] (in million lbs)
Crabs (Dungeness, King, Snow, and Southern tanner)	113	48	103
Pollock	90	38	3,368
Atka Mackerel, Sablefish, Goosefish, Pacific ocean perch	80	34	330
Squid	76	32	160
Tunas	18	7.5	59
Geoduck	15	6.4	8.4
Herrings	14	5.9	137

[1] Commodities with estimated trade damages of less than $5 million were not considered.
[2] Source: Trade Data Monitor.
[3] Source: NOAA fisheries

The STRP seafood payment rate is on a per pound basis as shown in the following table.

Seafood	Rate ($/lb.)
Atka mackerel	$0.10
Crab -Dungeness	0.47
Crab, King	0.47
Crab, Snow	0.47
Crab, Southern Tanner	0.47
Flounder	0.15
Geoduck	0.76
Goosefish	0.10
Herring	0.04
Lobster	0.50
Pacific Cod	0.14
Pacific Ocean Perch	0.10
Pollock	0.01
Sablefish	0.10
Salmon	0.16
Sole	0.15
Squid	0.20
Tuna	0.13
Turbot	0.15

Those payment rates reflect the estimated severity of the impact of trade disruptions to U.S. seafood caught and sold commercially, and the adjustment to new trade patterns for the types of seafood products identified in this document.

The actual production (in pounds) used to calculate an STRP payment under this document is not to exceed the 2019 reported commercial production in which the applicant had an ownership share (greater than zero shares) for seafood caught in U.S. territorial waters, including seafood caught in EEZs as authorized by treaties between the United States and Canada. The STRP payment, subject to the payment limit, will be calculated as follows:

Commercial Fisherman's Share of Production of Seafood Commodity (in pounds) × STRP Payment Rate

For example, a commercial fisherman submits an application specifying cod landings for 2019 as 375,000 pounds. FSA calculates the payment by multiplying 375,000 × $0.14.

Production Evidence

To apply for an STRP payment for seafood, on the application, the applicant commercial fisherman will certify the amount of commercial landings in pounds for the 2019 season. If requested by FSA, the commercial fisherman must also provide supporting documentation to provide production evidence for the amount and type of certified landings.

Examples of acceptable documentation for production evidence include: legal commercial fishing production records that are determined acceptable by the FSA county committee as verified by the appropriate Federal or State fishery management agency.

Paperwork Reduction Act Requirements

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35), FSA is requesting comments from interested individuals and organizations on the information collection activities related to STRP. After the 60-day period ends, the information collection request will be submitted to OMB for the 3-year approval to cover STRP information collection.

To start the STRP information collection approval, prior to publishing this document, FSA received emergency approval from OMB for 6 months. The emergency approval covers STRP information collection activities.

Title: Seafood Trade Relief Program (STRP).

OMB Control Number: 0560–New.

Type of Request: New Collection.

Abstract: This information collection is required to support all STRP information collection activities (applicable notifications published in the **Federal Register**) to provide payments to the eligible applicants, with respect to seafood that have been impacted by trade actions of foreign governments resulting in the loss of exports. The information collection is necessary to evaluate the application and other required paperwork for determining the commercial fisherman's eligibility and assist in commercial fisherman's payment calculations.

To start the STRP collection approval, FSA received emergency approval from OMB for 6 months. The emergency approval covers this NOFA and any other STRP information collection activities.

For the following estimated total annual burden on respondents, the formula used to calculate the total burden hour is the estimated average time per response multiplied by the estimated total annual responses.

Public reporting burden for this information collection is estimated to include the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed and completing and reviewing the collections of information.

Type of Respondents: Commercial fishermen.

Estimated Annual Number of Respondents: 43,000.

Estimated Number of Reponses per Respondent: 5.03.

Estimated Total Annual Responses: 216,300.

Estimated Average Time per Response: 0.399 hours.

Estimated Total Annual Burden on Respondents: 86,308 hours.

FSA is requesting comments on all aspects of this information collection to help us to:

(1) Evaluate whether the collection of information is necessary for the proper performance of the functions of the FSA, including whether the information will have practical utility;

(2) Evaluate the accuracy of the FSA's estimate of burden 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.

All comments received in response to this document, including names and addresses when provided, will be a matter of public record. Comments will be summarized and included in the submission for Office of Management and Budget approval.

Environmental Review

The environmental impacts for STRP have been considered in a manner consistent with the provisions of the National Environmental Policy Act (NEPA, 42 U.S.C. 4321–4347), the regulations of the Council on Environmental Quality (40 CFR parts 1500–1508), and the FSA regulation for compliance with NEPA (7 CFR part 799).

As previously stated, the intent of STRP is to provide financial assistance to commercial fishermen for expanding or aiding in the expansion of domestic markets for U.S. commercially caught and sold seafood, because seafood commodities have been impacted by trade actions of foreign governments resulting in the loss of exports. The limited discretionary aspects of STRP (for example, determining AGI and payment limitations) were designed to be consistent with established FSA and CCC programs, but also take into account certain differences associated with seafood production from crop production. These discretionary aspects do not have the potential to impact the human environment as they are administrative. Accordingly, the following Categorical Exclusions in 7 CFR part 799.31 apply:

- § 799.31(b)(6)(iii) applies to financial assistance to supplement income, manage the supply of agricultural commodities, or influence the cost and supply of such commodities; and
- § 799.31(b)(6)(iv) applies to individual farm participation in FSA programs where no ground disturbance or change in land use occurs as a result of the proposed action or participation.

No Extraordinary Circumstances (§ 799.33) exist. As such, the implementation of STRP and the participation in STRP do not constitute major Federal actions that would significantly affect the quality of the human environment, individually or cumulatively. Therefore, CCC will not prepare an environmental assessment or environmental impact statement for this action and this document serves as documentation of the programmatic environmental compliance decision for this federal action.

Federal Assistance Programs

The title and number of the Federal assistance programs, as found in the Catalog of Federal Domestic Assistance, to which this document applies is 10.131—Seafood Trade Relief Program.

Richard Fordyce,

Administrator, Farm Service Agency.

Robert Stephenson,

Executive Vice President, Commodity Credit Corporation.

[FR Doc. 2020–20143 Filed 9–9–20; 11:15 am]

BILLING CODE 3410–05–P

DEPARTMENT OF AGRICULTURE

Forest Service

Information Collection: Federal and Non-Federal Financial Assistance Instruments

AGENCY: Forest Service, Agriculture (USDA).

ACTION: Notice; request for comment.

SUMMARY: In accordance with the Paperwork Reduction Act of 1995, the Forest Service is seeking comments from all interested individuals and organizations on the adoption of a new form to replace multiple versions of a currently approved information collection, OMB 0596–0217, Federal and Non-Federal Financial Assistance Instruments.

DATES: Comments must be received in writing on or before November 13, 2020 to be assured of consideration. Comments received after that date will be considered to the extent practicable.

ADDRESSES: Comments concerning this notice should be addressed to Jacqueline Henry, USDA Forest Service, Director for Office of Grants and Agreements, 1400 Independence Ave. SW, Mailstop 1138, Washington, DC 20250.

Comments also may be submitted via facsimile to 703–605–4776 or by email to: *jacqueline.henry@usda.gov.*

The public may inspect comments received at USDA Forest Service, 1400 Independence Ave. SW, Washington, DC 20250, during normal business hours. Visitors are encouraged to call ahead to 703–605–4776 to facilitate entry to the building.

FOR FURTHER INFORMATION CONTACT: Jacqueline Henry, Director for Office of Grants and Agreements, telephone 703–605–4776.

Individuals who use telecommunication devices for the deaf (TDD) may call the Federal Relay Service (FRS) at 1–800–877–8339, 24 hours a day, 7 days a week, including holidays.

SUPPLEMENTARY INFORMATION:

Title: Federal and Non-Federal Financial Assistant Instruments.

OMB Number: 0596–0217.

Expiration Date of Approval: 11/30/2017.

Type of Request: Renewal with change.

Abstract: In order to perform specific Forest Service activities, Congress created several authorities to assist the Agency in carrying out its mission. The Forest Service issues partnership agreements under specific authorities exempt from the Federal Grants and Cooperative Agreements Act (FGCAA). This collection is for a new form that will be used to enter into the following agreement types by the Forest Service:

(1) Participating Agreements (replaces FS–1500–16 and 16A through 16G),

(2) Cost-Reimbursable Agreement (replaces FS–1500–12),

(3) Joint Venture Agreement (replaces FS–1500–14 and 14A),

(4) Cooperative Research and Development Agreements (replaces FS1500–13 through 13B); and,

(5) Challenge Cost-Share Agreement (replaces FS–1500–10 and 10A through 10C).

In addition to Federal Financial Assistance (FFA), Congress created specific authorizations for acts outside the scope of the FGCAA. Appropriations language was developed to convey authority for the Forest Service to enter into relationships that are outside the scope of the FGCAA. The Forest Service implements these authorizations using instruments such as collection agreements, FGCAA exempted agreements, memorandums of understanding, and other agreements which mutually benefit participating parties. These instruments fall outside the scope of the Federal Acquisition Regulations (FAR) and often require financial plans and statements of work. Forest Service employees collect information from cooperating parties from the pre-award to the closeout stage via telephone calls, emails, postal mail, and person-to-person meetings to create, develop, and administer these funded and non-funded agreements. The multiple means for respondents to communicate their responses include forms, non-forms, electronic documents, face-to-face, telephone, and internet. The scope of information collected varies; however, it typically includes the project type, project scope, financial plan, statement of work, and cooperator's business information.

The Forest Service would not be able to create, develop, and administer these funded and non-funded agreements without the collected information. The Agency would also be unable to develop or monitor projects, make or receive payments, or identify financial and accounting errors.

Estimate of Annual Burden: 1 to 4 hours annually per person.

Type of Respondents: Non-profit and for profit institutions; institutions of higher education; State, local, and Native American tribal governments, individuals; foreign governments; and organizations.

Estimated Annual Number of Respondents for New Form: 1,875.

Estimated Annual Number of Responses per Respondent: 1 to 4.

Estimated Total Annual Burden on Respondents: 7,500 hours.

Comment is invited on: (1) Whether this collection of information is necessary for the stated purposes and the proper performance of the functions of the Agency, including whether the information will have practical or scientific utility; (2) the accuracy of the Agency's estimate of the burden of 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 the use of automated, electronic, mechanical, or other technological collection techniques or other forms of information technology.

All comments received in response to this notice, including names and addresses when provided, will be a matter of public record. Comments will be summarized and included in the submission for Office of Management and Budget approval.

Jacqueline Henry,

Director, Grants and Agreements Policy.

[FR Doc. 2020–20195 Filed 9–11–20; 8:45 am]

BILLING CODE 3411–15–P

DEPARTMENT OF AGRICULTURE

Forest Service

Tongass National Forest, Thorne Bay Ranger District; Alaska; Twin Mountain II Timber Sale

AGENCY: Forest Service, Agriculture (USDA).

ACTION: Notice of intent to prepare an environmental impact statement.

SUMMARY: The Forest Service will prepare an Environmental Impact Statement (EIS) for the Twin Mountain II Timber Sale, which proposes to offer timber for harvest in the Staney and Red Bay areas within the Thorne Bay Ranger District, Tongass National Forest. The Proposed Action would offer for harvest about 42 million board feet of timber from approximately 3,000 acres. In addition, transportation management activities such as road construction, reconstruction, maintenance and decommissioning are proposed.

DATES: Comments concerning the scope of the analysis must be received by [October 14, 2020. The draft EIS is expected December 2020 and the final EIS is expected May 2021.

ADDRESSES: Send written comments to the Thorne Bay Ranger District, Attn: Twin Mountain II Timber Sale, P.O. Box 19001, Thorne Bay, Alaska, 99919. Comments may also be sent electronically to *https://cara.ecosystem management.org/Public/CommentInput?Project=58626,* or via facsimile to 907–828–3309. In all correspondence, include your name, address, and organization name if you are commenting as a representative of an organization.

FOR FURTHER INFORMATION CONTACT: Lucy Maldonado, Planning Staff, Thorne Bay Ranger District, P.O. Box 19001, Thorne Bay, Alaska 99919 or by phone at 907–828–3250.

Individuals who use telecommunication devices for the deaf (TDD) may call the Federal Information Relay Service (FIRS) at 1–800–877–8339 between 8 a.m. and 8 p.m., Eastern Time, Monday through Friday.

SUPPLEMENTARY INFORMATION: This EIS will tier to and incorporate by reference the 2016 Tongass Land and Resource Management Plan (Forest Plan) Amendment Final EIS. The project area is located on Prince of Wales Island, approximately 75 to 100 miles west of Ketchikan, Alaska, within the Staney and Red Bay areas of the Thorne Bay Ranger District, Tongass National.

Purpose and Need for Action

The purpose of the Twin Mountain II Timber Sale is to implement the 2016 Forest Plan direction to move the project area toward the desired future conditions described in the plan. More specifically, the purpose is to manage the timber resource for production of sawtimber and other wood products and to meet multiple resource objectives. There is a need to provide a sustainable level of forest products to contribute to the economic sustainability of the region. Providing old-growth timber would preserve a viable timber industry by providing timber volume in an economically efficient manner while providing jobs and opportunities for Southeast Alaska residents.

Proposed Action

The Forest Service proposes to make approximately 42 million board feet (MMBF) of old growth timber available to offer for harvest and construct and reconstruct roads in the Staney and Red Bay areas within the Thorne Bay Ranger District. Timber would be made available to offer for harvest up to 3,000 acres of old-growth forest in the Modified Landscape and Timber Production land use designation areas, using one or more timber sales that would be implemented over the course of 5 to 10 years. The proposed action includes about 1,800 acres of even-aged management and about 1,200 acres of uneven-aged management, with estimated volume for even-aged management being 32.4 MMBF and 9.6 MMBF for uneven-aged management. The proposed action includes approximately 3 miles of new National Forest System road construction, 11 miles of new temporary road construction, and the reconditioning of approximately 35 miles of existing roads. Existing rock quarries would be used as available or new quarries would be developed as necessary to provide materials for road construction. Existing log transfer facilities at El Capitan, Exchange Cove, Lab Bay, Naukati, and Winter Harbor could be used. Under the proposed action, no young growth timber is proposed to be made available for harvest and no activities would occur within designated roadless areas. No special timber cutting prescriptions around communities are included in the proposed action.

Responsible Official

The Responsible Official for this project is the Tongass Forest Supervisor, Earl Stewart.

Nature of Decision To Be Made

Given the purpose and need of the project, the Forest Supervisor will review alternatives and consider the environmental consequences of those alternatives in making his decisions, including: (1) Whether to select the proposed action or another alternative; (2) the effects of road construction, reconstruction, and closure; (3) mitigation measures and monitoring; and (4) whether there may be a significant restriction to subsistence resources.

Preliminary Issues

Preliminary concerns identified by the interdisciplinary team include: (1) Designing an economical timber sale(s) that contributes to meeting market demand; (2) effects of timber harvest and road construction on wildlife, including habitat, travel corridors, and subsistence use of deer; and (3) effects of timber harvest and road construction on watershed condition.

Permits or Licenses Required

All necessary permits will be obtained prior to project implementation.

Scoping Process

This notice of intent initiates the scoping process, which guides the development of the EIS. The Forest Service is soliciting internal and external input on the issues, impacts, and alternatives that will be addressed in the EIS. Scoping packages will be distributed to interested parties who have subscribed through an electronic mailing list to receive project information. Individuals and organizations wishing to subscribe may do so at: *https://public.govdelivery.com/accounts/USDAFS/subscriber/new?preferences=true.*

Additionally, there will be opportunities for involvement including open houses and subsistence hearings held in Prince of Wales Island communities. Project information, meeting announcements, notices, and documents will be provided on the project web page at: *http://www.fs.fed.us/nepa/nepa_project_exp.php?project=58626.*

Forest Service regulations at 36 CFR part 218, subparts A and B (78 FR18481–18504) regarding the project-level, predecisional administrative review process applies to projects and activities implementing land management plans. The Twin Mountain II Timber Sale is an activity implementing the Forest Plan and is subject to 36 CFR 218.

Only individuals or entities who submit timely and specific written comments concerning this project during this or other designated public comment periods established by the Responsible Official will be eligible to file an objection. It is important that reviewers provide their comments at such times and in such manner that they are useful to the agency's preparation of the EIS. Therefore, comments should be provided prior to the close of the comment period and should clearly articulate the reviewer's concerns and contentions.

Comments received in response to this solicitation, including names and addresses of those who comment, will be part of the public record for this proposed action. While comments submitted anonymously will be accepted and considered, they will not provide the submitters standing to participate in the predecisional review process.

Allen Rowley,

Associate Deputy Chief, National Forest System.

[FR Doc. 2020–20190 Filed 9–11–20; 8:45 am]

BILLING CODE 3411–15–P

DEPARTMENT OF COMMERCE

Foreign-Trade Zones Board

[B–29–2020]

Foreign-Trade Zone (FTZ) 148—Knoxville, Tennessee; Authorization of Production Activity; CoLinx, LLC; (Tapered Roller Bearing Unit and Gearhead Kitting) Crossville, Tennessee

On May 7, 2020, CoLinx, LLC (CoLinx) submitted a notification of proposed production activity to the FTZ Board for its facility within FTZ 148, in Crossville, Tennessee.

The notification was processed in accordance with the regulations of the FTZ Board (15 CFR part 400), including notice in the **Federal Register** inviting public comment (85 FR 29397–29398, May 15, 2020). On September 4, 2020, the applicant was notified of the FTZ Board's decision that no further review of the activity is warranted at this time. The production activity described in the notification was authorized, subject to the FTZ Act and the FTZ Board's regulations, including Section 400.14.

Dated: September 4, 2020.

Andrew McGilvray,

Executive Secretary.

[FR Doc. 2020–20219 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–DS–P

DEPARTMENT OF COMMERCE

Foreign-Trade Zones Board

[B–57–2020]

Foreign-Trade Zone (FTZ) 7—Mayaguez, Puerto Rico; Notification of Proposed Production Activity; Patheon Puerto Rico, Inc. (Pharmaceutical Products); Manatí, Puerto Rico

Patheon Puerto Rico, Inc. (Patheon), submitted a notification of proposed production activity to the FTZ Board for its facility in Manatí, Puerto Rico. The notification conforming to the requirements of the regulations of the FTZ Board (15 CFR 400.22) was received on September 2, 2020.

Patheon already has authority to produce certain pharmaceutical products within Subzone 7L. The current request would add a foreign status material to the scope of authority. Pursuant to 15 CFR 400.14(b), additional FTZ authority would be limited to the specific foreign-status material described in the submitted notification (as described below) and subsequently authorized by the FTZ Board.

Production under FTZ procedures could exempt Patheon from customs duty payments on the foreign-status material used in export production. On its domestic sales, for the foreign-status material noted below, Patheon would be able to choose the duty rates during customs entry procedures that apply to its already authorized finished products (duty-free). Patheon would be able to avoid duty on the foreign-status material which becomes scrap/waste. Customs duties also could possibly be deferred or reduced on foreign-status production equipment.

The material sourced from abroad is microcrystalline cellulose (duty rate 5.2%). The request indicates that microcrystalline cellulose is subject to duties under Section 301 of the Trade Act of 1974 (Section 301), depending on the country of origin. The applicable Section 301 decisions require subject merchandise to be admitted to FTZs in privileged foreign status (19 CFR 146.41).

Public comment is invited from interested parties. Submissions shall be addressed to the Board's Executive Secretary and sent to: *ftz@trade.gov.* The closing period for their receipt is October 26, 2020.

A copy of the notification will be available for public inspection in the ''Reading Room'' section of the Board's website, which is accessible via *www.trade.gov/ftz.*

For further information, contact Christopher Wedderburn at *Chris.Wedderburn@trade.gov* or (202) 482–1963.

Dated: September 9, 2020.

Elizabeth Whiteman,

Acting Executive Secretary.

[FR Doc. 2020–20216 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–DS–P

DEPARTMENT OF COMMERCE

Foreign-Trade Zones Board

[B–30–2020]

Foreign-Trade Zone (FTZ) 183—Austin, Texas; Authorization of Production Activity; Rohr, Inc. (Aircraft Engine Parts); San Marcos, Texas

On May 8, 2020, Rohr, Inc. submitted a notification of proposed production activity to the FTZ Board for its facility within Subzone 183D, in San Marcos, Texas.

The notification was processed in accordance with the regulations of the FTZ Board (15 CFR part 400), including notice in the **Federal Register** inviting public comment (85 FR 30928, May 21, 2020). On September 8, 2020, the applicant was notified of the FTZ Board's decision that no further review of the activity is warranted at this time. The production activity described in the notification was authorized, subject to the FTZ Act and the FTZ Board's regulations, including Section 400.14.

Dated: September 8, 2020.

Elizabeth Whiteman,

Acting Executive Secretary.

[FR Doc. 2020–20217 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–DS–P

DEPARTMENT OF COMMERCE

Foreign-Trade Zones Board

[B–31–2020]

Foreign-Trade Zone (FTZ) 82—Mobile, Alabama; Authorization of Production Activity; Rohr, Inc. (Aircraft Engine Parts); Foley and Loxley, Alabama

On May 8, 2020, Rohr, Inc. submitted a notification of proposed production activity to the FTZ Board for its facilities within Subzone 82J, in Foley and Loxley, Alabama.

The notification was processed in accordance with the regulations of the FTZ Board (15 CFR part 400), including notice in the **Federal Register** inviting public comment (85 FR 30928–30929, May 21, 2020). On September 8, 2020, the applicant was notified of the FTZ Board's decision that no further review of the activity is warranted at this time. The production activity described in the notification was authorized, subject to the FTZ Act and the FTZ Board's regulations, including Section 400.14.

Dated: September 8, 2020.

Elizabeth Whiteman,

Acting Executive Secretary.

[FR Doc. 2020–20218 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–DS–P

DEPARTMENT OF COMMERCE

International Trade Administration

Announcement of Upcoming US–UK Financial Innovation Partnership (FIP) Trade Mission to the United Kingdom and Education Trade Mission to India

AGENCY: International Trade Administration, Department of Commerce.

SUMMARY: The United States Department of Commerce, International Trade Administration (ITA) is announcing two upcoming trade missions that will be recruited, organized, and implemented by ITA. These missions are: US-UK Financial Innovation Partnership Trade Mission to the United Kingdom—June 21–24, 2021; Education Trade Mission to India—August 2–7, 2021. A summary of each mission is found below. Application information and more detailed mission information, including the commercial setting and sector information, can be found at the trade mission website: *https://www.trade.gov/trade-missions.* For each mission, recruitment will be conducted in an open and public manner, including publication in the **Federal Register**, posting on the Commerce Department trade mission calendar (*https://www.trade.gov/trade-missions-schedule*) and other internet websites, press releases to general and trade media, direct mail, broadcast fax, notices by industry trade associations and other multiplier groups, and publicity at industry meetings, symposia, conferences, and trade shows.

FOR FURTHER INFORMATION CONTACT: Gemal Brangman, Trade Promotion Programs, Industry and Analysis, International Trade Administration, U.S. Department of Commerce, 1401 Constitution Avenue NW, Washington, DC 20230; telephone (202) 482–3773.

SUPPLEMENTARY INFORMATION:

The Following Conditions for Participation Will Be Used for Each Mission

Applicants must submit a completed and signed mission application and supplemental application materials, including adequate information on their products and/or services, primary market objectives, and goals for participation to allow the Department of Commerce to evaluate their application. If the Department of Commerce receives an incomplete application, the Department may either: reject the application, request additional information/clarification, or take the lack of information into account when evaluating the application. If the requisite minimum number of participants is not selected for the mission by the recruitment deadline, the mission may be cancelled.

Each applicant must also certify that the products and services it seeks to export through the mission are either produced in the United States, or, if not, are marketed under the name of a U.S. firm and have at least 51% U.S. content by value. In the case of an organization, the applicant must certify that, for each entity to be represented by the organization, the products and/or services the represented firm or service provider seeks to export are either produced in the United States or, if not, marketed under the name of a U.S. firm and have at least 51% U.S. content.

An organization applicant must certify to the above for all of the companies it seeks to represent on the mission.

In addition, each applicant must:

- Certify that the export of products and services that it wishes to market through the mission is in compliance with U.S. export controls and regulations;
- Certify that it has identified any matter pending before any bureau or office in the Department of Commerce;
- Certify that it has identified any pending litigation (including any administrative proceedings) to which it is a party that involves the Department of Commerce; and
- Sign and submit an agreement that it and its affiliates (1) have not and will not engage in the bribery of foreign officials in connection with a company's/participant's involvement in this mission, and (2) maintain and enforce a policy that prohibits the bribery of foreign officials.

In the case of a trade association/organization, the applicant must certify that each firm or service provider to be represented by the association/organization can make the above certifications.

The Following Selection Criteria Will Be Used for Each Mission

Targeted mission participants are U.S. firms, services providers and organizations (universities, research institutions, or financial services trade associations) providing or promoting U.S. products and services that have an interest in entering or expanding their business in the mission's destination country. The following criteria will be evaluated in selecting participants:

- Suitability of the applicant's (or in the case of an organization, represented firm's or service provider's) products or services to these markets;
- The applicant's (or in the case of an organization, represented firm's or service provider's) potential for business in the markets, including likelihood of exports resulting from the mission; and
- Consistency of the applicant's (or in the case of an organization, represented firm's or service provider's) goals and objectives with the stated scope of the mission.

Balance of applicant's size and location may also be considered during the review process.

Referrals from a political party or partisan political group or any information, including on the application, containing references to political contributions or other partisan political activities will be excluded from the application and will not be considered during the selection process. The sender will be notified of these exclusions.

Trade Mission Participation Fees

If and when an applicant is selected to participate on a particular mission, a payment to the Department of Commerce in the amount of the designated participation fee below is required. Upon notification of acceptance to participate, those selected have 5 business days to submit payment or the acceptance may be revoked.

Participants selected for a trade mission will be expected to pay for the cost of personal expenses, including, but not limited to, international travel, lodging, meals, transportation, communication, and incidentals, unless otherwise noted. Participants will, however, be able to take advantage of U.S. Government rates for hotel rooms. In the event that a mission is cancelled, no personal expenses paid in anticipation of a mission will be reimbursed. However, participation fees for a cancelled mission will be reimbursed to the extent they have not already been expended in anticipation of the mission.

If a visa is required to travel on a particular mission, applying for and obtaining such a visa will be the responsibility of the mission participant. Government fees and processing expenses to obtain such a visa are not included in the participation fee. However, the Department of Commerce will provide instructions to each participant on the procedures required to obtain business visas.

Trade Mission members participate in trade missions and undertake mission-related travel at their own risk. The nature of the security situation in a given foreign market at a given time cannot be guaranteed. The U.S. Government does not make any representations or guarantees as to the safety or security of participants. The U.S. Department of State issues U.S. Government international travel alerts and warnings for U.S. citizens available at *https://travel.state.gov/content/travel/en/traveladvisories/traveladvisories.html/*. Any question regarding insurance coverage must be resolved by the participant and its insurer of choice.

Definition of Small- and Medium-Sized Enterprise

For purposes of assessing participation fees, an applicant is a small or medium-sized enterprise (SME) if it qualifies under the Small Business Administration's (SBA) size standards (*https://www.sba.gov/document/support--table-size-standards*), which vary by North American Industry Classification System (NAICS) Code. The SBA Size Standards Tool [*https://www.sba.gov/size-standards/*] can help you determine the qualifications that apply to your company.

Mission List: (additional information about each mission can be found at *https://www.trade.gov/trade-missions*).

U.S.-UK Financial Innovation Partnership Trade Mission to the United Kingdom

Dates: June 21–24, 2021

Summary

The United States Department of Commerce, International Trade Administration (ITA) is organizing a financial services trade mission to the United Kingdom in conjunction with the United States-United Kingdom Financial Innovation Partnership Initiative from June 21 to 24, 2021.

The purpose of the U.S.-UK Financial Innovation Partnership (FIP) trade mission is to expand opportunities for U.S. companies at the intersection of financial services, technology and international commerce. The FIP was established in May 2019 with the intent of encouraging collaboration in the private sector, sharing information and expertise about regulatory practices, and promoting growth and innovation. The FIP focuses on two main areas—regulatory engagement and commercial engagement. The FIP also seeks to promote a dynamic private sector that supports entrepreneurs and new business models—a necessary driver of financial innovation. The FIP was specifically mentioned during the first round of U.S.-UK Free Trade Agreement negotiations in May 2020, as an important bilateral dialogue that reflects a bilateral commitment to open markets and the importance of the financial services sector.

The FIP commercial engagement pillar provides for enhanced and regular opportunities for the private sector in one country to engage with industry associations and market participants in the other country. Participants in the FIP Trade Mission will gain market insights, make industry contacts, solidify business strategies, and discuss enabling policies, with the primary goal of increasing U.S. exports of products and services to the UK. The FIP mission will include, where available, customized business appointments with pre-screened potential business partners, such as buyers, agents, distributors and/or joint venture partners; meetings with subnational and/or local government officials and industry leaders; and networking events.

Proposed Timetable

Monday, June 21, 2021	• Trade Mission Participants Arrive. • No Host Dinner/Delegation Meet Up/Evening Activity (i.e., London Eye).
Tuesday, June 22, 2021	• Opening Breakfast at Winfield House (Regents Park). • FCA Sandbox Discussion (Stratford). • Level 39 Accelerator Show Round and Visit with Key Tenants (Canary Wharf). • Evening Reception—TBC Bank/Venue in Canary Wharf.
Wednesday, June 23, 2021	• 7:30 am Opening of London Stock Exchange Networking, Ceremony, and Information on Listing on the Exchange (St Paul's).

	• Bank of England Show Round and Discussion (Bank). • Delegation: Lunch on Own (Bank/Various); DAS: Programming with DIT Counterparts (Whitehall). • FIP Roundtable Discussion with HMG, FinTech Alliance at U.S. Embassy (Vauxhall). • Evening Reception (Sponsored/Venue TBC).
Thursday, June 24, 2021	• Pitch Fest Half Day Forum at U.S. Embassy (Vauxhall). • *Official Trade Mission Program Concludes.*

* **Note:** The final schedule and potential site visits will depend on the availability of host government and business officials, specific goals of mission participants, and ground transportation.

Participation Requirements

All parties interested in participating in the trade mission must complete and submit an application package for consideration by the Department of Commerce. All applicants will be evaluated on their ability to meet certain conditions and best satisfy the selection criteria as outlined below. A minimum of 10 and maximum of 15 firms and/or trade associations will be selected to participate in the mission from the applicant pool.

Fees and Expenses

After a firm or trade association has been selected to participate on the mission, a payment to the Department of Commerce in the form of a participation fee is required. The participation fee for the United States—United Kingdom Financial Innovation Partnership (FIP) trade mission will be $2,800 for small or medium-sized enterprises (SMEs); and $4,500 for large firms or organization. The fee for each additional firm representative (large firm or SME/trade organization) is $750. When an applicant is selected to participate on the mission, a payment to the Department of Commerce in the amount of the designated participation fee is required. Upon notification that they have been selected to participate, those selected have 5 business days to submit payment or the acceptance may be revoked.

Timeframe for Recruitment and Application

Mission recruitment will be conducted in an open and public manner, including publication in the **Federal Register**, posting on the Commerce Department trade mission calendar (*https://www.trade.gov/trade-missions-schedule*) and other internet websites, press releases to general and trade media, direct mail, notices by industry trade associations and other multiplier groups, and publicity at industry meetings, symposia, conferences, and trade shows. Recruitment for the mission will begin immediately and conclude no later than December 18, 2020. The U.S. Department of Commerce will review applications and inform applicants of selection decisions on a comparative basis. Applications received after December 18, 2020, will be considered only if space and scheduling constraints permit.

Contacts

Doreen Parekh, Lead, Finance and Innovation, Office of Finance and Insurance Industries, Washington, DC, (202) 482–2915, *Doreen.Parekh@trade.gov.*

Gemal Brangman, Senior Advisor, Trade Missions, Trade Events Management Task Force, Washington, DC, (202) 482–3773, *Gemal.Brangman@trade.gov.*

Chrystal Denys, Commercial Specialist, U.S. Commercial Service London, +44 (0) 207 891 3419, *Chrystal.Denys@trade.gov.*

Peter Sexton, Director, Global Financial Services Team, U.S. Commercial Service New York City, (212) 809–2647, *PeterSexton@trade.gov.*

Eli Corso-Phinney, International Trade Specialist, Office of Western and Northern Europe, Washington, DC, (202) 482–7941, *Eli.Corso-Phinney@trade.gov.*

Vincent Tran, International Trade Specialist, Office of Finance and Insurance Industries, Washington, DC, (202) 482–2967, *Vincent.Tran@trade.gov.*

Brian Beams, Deputy Team Leader Financial Services, U.S. Commercial Service Northern New Jersey, (862) 235–5267, *Brian.Beams@trade.gov.*

Ryan Wallace, Senior International Investment Specialist, SelectUSA, (202) 482–7805, *Ryan.Wallace@trade.gov.*

Education Trade Mission to India

Dates: August 2–7, 2021

Summary

The United States Department of Commerce, International Trade Administration, U.S. Commercial Service is organizing an education industry trade mission to three cities in India: New Delhi, Bengaluru and Mumbai from August 2 to 7, 2021. This mission will include representatives from regionally accredited graduate and undergraduate schools, educational technology companies, and state study consortia whose members are also appropriately accredited at the regional level. This mission will seek to connect U.S. educational institutions and businesses operating in the educational sector to potential students, university/institution partners, and education consultants in India. The mission will include one-on-one appointments with potential partners, embassy briefings, and student fairs and networking events in New Delhi, Bengaluru, and Mumbai to recruit Indian students to the United States.

In addition to the three cities in the mission, participants may choose optional spin offs in up to four markets (Kolkata, Ahmedabad, Hyderabad and Chennai) in India, for business-to-business meetings.

Proposed Timetable

New Delhi	Travel Day/Arrival in New Delhi. *Optional No Host Cultural Activities*.
Monday, August 2, 2021	New Delhi: Briefing, One-on-One matchmaking meetings; Hosted Lunch; Evening: Icebreaker Reception.
Tuesday, August 3, 2021	Half day site visit—or student fair; Late afternoon departure for Bengaluru.
Bengaluru	Travel Day/Arrival in Bengaluru. Optional Local Tour/Activities.
Wednesday, August 4, 2021	Bengaluru: Briefing, One-on-One matchmaking meetings; Hosted Lunch.
Thursday, August 5, 2021	Half day site visit—or student fair; Late afternoon departure for Mumbai.
Mumbai	Travel Day/Arrival in Mumbai. *Optional No Host Cultural Activities*.
Friday, August 6, 2021	Mumbai: Briefing, One-on-One matchmaking meetings; Hosted Lunch. Student fair.
Saturday, August 7, 2021	Half day site visit—or partner event; Evening Wheels-up.

Participation Requirements

All parties interested in participating in the U.S. Department of Commerce Education Trade Mission to India must complete and submit an application package for consideration by the Department of Commerce. All applicants will be evaluated on their ability to meet certain conditions and best satisfy the selection criteria as outlined below.

A minimum of 15 and a maximum of 30 educational institutions/study state consortia/companies will be selected to participate in the mission. All selected participants will travel to three cities in India and will have the option to choose additional business-to-business side meetings in up to four markets in India as a spinoff for an additional cost.

The Trade Mission is open to U.S. educational institutions/study state consortia/U.S. educational technology companies that are new to India and those with existing business in India that are seeking to expand their market share. U.S. educational technology companies should offer unique, state-of-the-art, innovative solutions.

Fees and Expenses

After an educational institution/study state consortium/company has been selected to participate on the mission, a payment to the Department of Commerce in the form of a participation fee is required.

For the trade mission, the participation fee will be $4,326 for a small- or medium-sized enterprise (SME)* and $5,915 for large firms. Additional participants representing the same institution may participate for a fee of $500 each. Participants who choose the optional spinoff opportunity for additional business-to-business meetings in up-to four markets (Kolkata, Ahmedabad, Hyderabad and Chennai) in India, can participate for a fee of $950 per city.

The mission registration fee includes market briefings, U.S. Embassy officer consultations, networking receptions, lunch and coffee breaks, as well as transportation associated with the mission program in the region.

Timeframe for Recruitment and Application

Mission recruitment will be conducted in an open and public manner, including publication in the **Federal Register**, posting on the Commerce Department trade mission calendar on *https://www.trade.gov/trade-missions-schedule* and other internet websites, press releases to the general and trade media, direct mail and broadcast fax, notices by industry trade associations and other multiplier groups and announcements at industry meetings, symposia, conferences, and trade shows.

Recruitment for the mission will begin immediately and conclude no later than June 30, 2021. The U.S. Department of Commerce will review applications and make selection decisions on a rolling basis until the maximum of 30 participants are selected. After the close of the recruitment period, educational institutions/study state consortia/companies will be considered only if space and scheduling constraints permit.

Contacts

Gabriel Zelaya, Global Education Team Leader, U.S. Commercial Service—San Jose/Silicon Valley, U.S. Department of Commerce, *gabriela.zelaya@trade.gov,* Tel: 408–335–9202.

India Contact Information

Brenda VanHorn, Principal Commercial Officer, U.S. Commercial Service—U.S. Consulate General, Mumbai, *Brenda.Vanhorn@trade.gov.*

Noella Monteiro, Commercial Advisor, U.S. Commercial Service—U.S. Consulate General, Mumbai, *Noella.Monteiro@trade.gov.*

Dated: September 8, 2020.

Gemal Brangman,

Senior Advisor, Trade Missions, ITA Events Management Task Force.

[FR Doc. 2020–20154 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–DR–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[RTID 0648–XA480]

New England Fishery Management Council; Public Meeting

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of public meeting.

SUMMARY: The New England Fishery Management Council (Council, NEFMC) will hold a three-day meeting to consider actions affecting New England fisheries in the exclusive economic zone (EEZ). Due to federal and state travel restrictions and updated guidance from the Centers for Disease Control and Prevention related to COVID–19, this meeting will be conducted entirely by webinar.

DATES: The webinar meeting will be held on Tuesday, Wednesday, and Thursday, September 29, September 30, and October 1, 2020, beginning at 9 a.m. on September 29 and 8:30 a.m. on September 30 and October 1.

ADDRESSES: All meeting participants and interested parties can register to join the webinar at *https://register.gotowebinar.com/register/5172076717962269709.*

Council address: New England Fishery Management Council, 50 Water Street, Mill 2, Newburyport, MA 01950; telephone: (978) 465–0492; *www.nefmc.org.*

FOR FURTHER INFORMATION CONTACT: Thomas A. Nies, Executive Director, New England Fishery Management Council; telephone: (978) 465–0492, ext. 113.

SUPPLEMENTARY INFORMATION:

Agenda

Tuesday, September 29, 2020

After introductions and brief announcements, NMFS's Regional Administrator for the Greater Atlantic Regional Fisheries Office (GARFO) will swear in new and reappointed Council members. The Council then will conduct its 2020–21 election of officers. Reports on recent activities will be next. The Council will hear from its Chairman and Executive Director, GARFO's Regional Administrator, liaisons from the Northeast Fisheries Science Center (NEFSC) and Mid-Atlantic Fishery Management Council, staff from the Atlantic States Marine Fisheries Commission (ASMFC), and representatives from NOAA General Counsel, NOAA's Office of Law Enforcement, the U.S. Coast Guard, the Northeast Trawl Advisory Panel (NTAP), the Northwest Atlantic Fisheries Organization (NAFO), the NMFS Highly Migratory Species Advisory Panel, and the South Atlantic Council's Dolphin/Wahoo Advisory Panel. The Skate Committee Report will follow. The Council will receive: (1) A presentation on the Skate Annual Monitoring Report covering fishing year 2019; and (2) a progress report on Amendment 5 to the Northeast Skate Complex Fishery Management Plan (FMP). This update will focus on the development of a problem statement, goals, and objectives for potentially developing a limited access program through Amendment 5. Members of the public then will have the opportunity to speak during an open comment period on issues that relate to Council business but are not included on the published agenda for this meeting. The Council asks the public to limit remarks to 3–5 minutes. These comments will be received through the webinar. A guide for how to publicly comment through the webinar is available on the Council website at *https://s3.amazonaws.com/nefmc.org/NEFMC-meeting-remote-participation_generic.pdf.*

Following the lunch break, the Council will receive a report from the Northeast Fisheries Science Center on the peer review of the Spring 2020 Management Track Stock Assessments for Atlantic herring, longfin squid, butterfish, and surfclams and ocean quahogs. The Scientific and Statistical Committee (SSC) then will present its recommendations for overfishing limits (OFLs) and acceptable biological catches (ABCs) for the 2021–2023 Atlantic herring fishing years. The Atlantic Herring Committee report will be next with three items: (1) The Council will take final action on Framework Adjustment 8, which includes 2021–2023 specifications for the herring fishery and adjusts measures in the Atlantic Herring FMP that may inhibit the Atlantic mackerel fishery from achieving optimum yield; (2) the Council will receive an update on Framework Adjustment 7, which is an action under development to protect spawning herring on Georges Bank; and (3) the Council will receive an update on discussions related to the coordination of Atlantic herring management between the Council and ASMFC. GARFO then will update the Council on the status of the North Atlantic Right Whale Draft Biological Opinion and upcoming rulemaking. The Council may discuss these issues and offer comments to the agency. After that, the Council will adjourn for the day.

At 6 p.m. or shortly following the close of Council business, the U.S. International Trade Commission (USITC) will host a virtual roundtable to gather input from New England fishermen and other industry stakeholders on two topics: (1) The impacts of illegal, unreported, and unregulated (IUU) fishing on the U.S. fishing industry; and (2) the impacts of seafood imports on U.S. products and markets. All stakeholders, including those from the Mid-Atlantic, are encouraged to join the discussion. No preregistration is needed. A link to the webinar will be forthcoming and posted on the Council website.

Wednesday, September 30, 2020

The Council will begin the day with Part 1 of a three-part Groundfish Committee report. Part 1 will focus on Amendment 23 to the Northeast Multispecies FMP, commonly referred to as the groundfish monitoring amendment. The Council will review all written and oral comments received during the public comment period on this amendment and then take final action on measures to improve the accuracy and accountability of catch reporting in the commercial groundfish fishery, including the level of at-sea monitoring coverage to be required on groundfish sector trips, among other actions.

Following the lunch break, the Council will continue its discussion on Groundfish Monitoring Amendment 23. When business on the amendment is complete, the Council will take up Part 2 of the Groundfish Committee Report regarding a petition for rulemaking for Atlantic cod. The Council will receive input from its Groundfish Committee, Groundfish Advisory Panel, and Recreational Advisory Panel and then discuss the petition and potential next steps. After that, the Council will: (1) Receive a report from the Transboundary Resources Assessment Committee (TRAC) on 2020 assessment results for Eastern Georges Bank cod, Eastern Georges Bank haddock, and Georges Bank yellowtail flounder; and (2) review and approve Transboundary Management Guidance Committee (TMGC) recommendations for 2021 total allowable catches for those three shared U.S./Canada stocks on Georges Bank. Next, the Council will receive SSC recommendations for OFLs and ABCs for Georges Bank yellowtail flounder for fishing years 2021 and 2022, as well as SSC input on possible rebuilding approaches for white hake. Finally, the Council will take up Part 3 of the Groundfish Committee report, which will focus on Framework Adjustment 61 to the Northeast Multispecies FMP. The framework includes: (1) 2021 total allowable catches for U.S./Canada stocks on Georges Bank; (2) 2021–23 specifications for roughly half of the U.S. groundfish stocks; (3) white hake rebuilding provisions; and (4) other measures. The Council also will take action on Georges Bank yellowtail OFLs and ABCs for Framework 61 before it adjourns for the day.

Thursday, October 1, 2020

The Council will begin the day by receiving a short update from the Habitat Committee on offshore wind development activities. Then it will take up the Scallop Committee report. The Council will review recent public hearing comments on Amendment 21 to the Atlantic Sea Scallop FMP, which includes measures that address: (1) Northern Gulf of Maine Management Area issues, (2) the Limited Access General Category (LAGC) possession limit, and (3) individual fishing quota (IFQ) transfers. The Council will take final action on this amendment. The Council also will receive a preliminary overview of 2020 scallop survey work and a progress report on Framework Adjustment 33, which will include 2021 fishing year specifications and 2022 default specifications, along with other measures.

Following the lunch break, the Council will hear from its Ecosystem-Based Fishery Management (EBFM) Committee. First, the Council will review and approve EBFM public outreach materials produced by Green Fin Studio, including stakeholder profiles, brochures, two completed infographics, presentations, an introductory video, and other outreach tools. Second, the Council will hear the committee's recommendations and approve a format for conducting EBFM workshops using the Council's example Fishery Ecosystem Plan (eFEP) for Georges Bank, along with the new public outreach materials. Third, the Council will receive a presentation on tangible worked examples developed by the Plan Development Team to demonstrate the eFEP catch framework for Georges Bank. Next, the Council will hear from the Stellwagen Bank National Marine Sanctuary (SBNMS) staff, which will present two pre-COVID0919 economic reports supporting the SBNMS Management Plan Review: (1) A fisheries report analyzing commercial fishing and recreational for-hire fishing activity within SBNMS and the economic contributions of these activities; and (2) a whale watching report summing up data and economic contribution. After that, the Council will begin its initial discussion on 2021 Council Priorities, including identification of potential actions that respond to the May 7, 2020 Executive Order on Promoting American Seafood Competitiveness and Economic Growth. The Council then will close out the meeting with other business.

Although non-emergency issues not contained on this agenda may come before the Council for discussion, those issues may not be the subject of formal action during this meeting. Council action will be restricted to those issues specifically listed in this notice and any issues arising after publication of this notice that require emergency action under section 305(c) of the Magnuson-Stevens Fishery Conservation and Management Act, provided the public has been notified of the Council's intent to take final action to address the emergency. The public also should be aware that the meeting will be recorded. Consistent with 16 U.S.C. 1852, a copy of the recording is available upon request.

Special Accommodations

This meeting is being conducted entirely by webinar. Requests for auxiliary aids should be directed to Thomas A. Nies (see **ADDRESSES**) at least 5 days prior to the meeting date.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: September 9, 2020.

Tracey L. Thompson,

Acting Deputy Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–20208 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

Agency Information Collection Activities; Submission to the Office of Management and Budget (OMB) for Review and Approval; Comment Request; Alaska Region Arbitration (Crab)

AGENCY: National Oceanic & Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of information collection; request for comment.

SUMMARY: The Department of Commerce, in accordance with the Paperwork Reduction Act of 1995 (PRA), invites the general public and other Federal agencies to comment on proposed, and continuing information collections, which helps us assess the impact of our information collection requirements and minimize the public's reporting burden. The purpose of this notice is to allow for 60 days of public comment preceding submission of the collection to OMB.

DATES: To ensure consideration, comments regarding this proposed information collection must be received on or before November 13, 2020.

ADDRESSES: Interested persons are invited to submit written comments to Adrienne Thomas, NOAA PRA Officer, at *Adrienne.thomas@noaa.gov.* Please reference OMB Control Number 0648–0516 in the subject line of your comments. Do not submit Confidential Business Information or otherwise sensitive or protected information.

FOR FURTHER INFORMATION CONTACT: Requests for additional information or specific questions related to collection activities should be directed to Gabrielle Aberle, 907–586–7356.

SUPPLEMENTARY INFORMATION:

I. Abstract

The National Marine Fisheries Service (NMFS), Alaska Regional Office, is requesting renewal of a currently approved information collection. This information collection contains the reports for the Crab Rationalization Program Arbitration System.

The Crab Rationalization Program allocates Bering Sea and Aleutian Islands (BSAI) crab resources among harvesters, processors, and coastal communities through a limited access system that balances the interests of these groups who depend on these fisheries. Under the CR Program, eligible License Limitation Program license holders were issued crab quota shares (QS), which are long term shares, based on their qualifying harvest histories. The QS yield annual individual fishing quota (IFQ), which represent a privilege to receive a certain amount of crab harvested with IFQ. Processor quota shares (PQS) are long term shares issued to processors. The PQS yield annual individual processor quota (IPQ), which represent a privilege to receive a certain amount of crab harvested with Class A IFQ.

The Crab Rationalization Program Arbitration System is a series of steps that harvesters and processors can use to negotiate delivery and price contracts. The Arbitration System allows unaffiliated Class A IFQ holders to initiate an arbitration proceeding in the event of a dispute to allow an independent third party to provide a review of harvester and processor negotiation positions and provide an independent and binding resolution to issues under dispute. To use the Arbitration System, a harvester must commit deliveries to a processor and initiate a binding arbitration proceeding in advance of the season opening. The Arbitration System is designed to minimize antitrust risks for crab harvesters and processors and is intended to ensure that a reasonable price is paid for all landings.

The Arbitration System requires several information collections that are submitted annually in accordance with the regulations at 50 CFR 680.20. The Annual Arbitration Organization Report, the Market Report, and the Non-binding Price Formula Report are the primary reports submitted to NMFS each year. Also submitted are the Contract Arbitrator Report and the Cost Allocation Agreement.

An Annual Arbitration Organization Report is compiled by each of the two Arbitration Organizations; one represents the processors, and the second represents the harvesters. This report includes information on the arbitration organization and its management personnel, the crab QS fisheries to which the report applies, the ownership interest and the QS/IFQ or PQS/IPQ held by each member; and the arbitration process.

The Non-binding Price Formula Report is a pre-season report that is designed to serve as a starting point for negotiations between fishermen and processors, or as a starting point for an arbitrator in evaluating offers in an arbitration process. This report documents how each formula was developed.

The Market Report provides an analysis of the market for products of a specific crab fishery and reports on activities occurring within three months prior to its generation. The purpose of this report is to provide background information on each crab fishery, the products generated by each fishery, and position of those products in the marketplace; discuss the historical division of wholesale revenue; and provide the methods for predicting wholesale prices before the fishery occurs.

The Contract Arbitrator Report documents arbitration proceedings if they occur within a fishery. The Cost Allocation Agreement provides combined shared arbitration accounting costs. Federal regulations for the CR Program require that the crab arbitration costs are shared equally between IPQ holders and Class A IFQ holders—processors pay half and fishermen pay half.

II. Method of Collection

The information is submitted by mail, delivery, fax, or email.

III. Data

OMB Control Number: 0648–0516.

Form Number(s): None.

Type of Review: Regular submission (extension of a current information collection).

Affected Public: Individuals or households; Business or other for-profit organizations.

Estimated Number of Respondents: 2.

Estimated Time per Response: Annual Arbitration Organization Report, 6 hours; Market Report, Nonbinding Price Formula Report, Contract Arbitrator Report, and Cost Allocation Agreement, 3 hours each.

Estimated Total Annual Burden Hours: 24.

Estimated Total Annual Cost to Public: $157,701 in recordkeeping/reporting costs.

Respondent's Obligation: Required to Obtain or Retain Benefits.

Legal Authority: Magnuson-Stevens Fishery Conservation and Management Act (16 U.S.C. 1801 *et seq.*)

IV. Request for Comments

We are soliciting public comments to permit the Department/Bureau to: (a) Evaluate whether the proposed information collection is necessary for the proper functions of the Department, including whether the information will have practical utility; (b) Evaluate the accuracy of our estimate of the time and cost burden for this proposed collection, including the validity of the methodology and assumptions used; (c) Evaluate ways to enhance the quality, utility, and clarity of the information to be collected; and (d) Minimize the reporting burden on those who are to respond, including the use of automated collection techniques or other forms of information technology.

Comments that you submit in response to this notice are a matter of public record. We will include or summarize each comment in our request to OMB to approve this ICR. Before including your address, phone number, email address, or other personal identifying information in your comment, you should be aware that your entire comment—including your personal identifying information—may be made publicly available at any time. While you may ask us in your comment to withhold your personal identifying information from public review, we cannot guarantee that we will be able to do so.

Sheleen Dumas,

Department PRA Clearance Officer, Office of the Chief Information Officer, Commerce Department.

[FR Doc. 2020–20200 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[RTID 0648–XA456]

Endangered and Threatened Species; Take of Anadromous Fish

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of availability.

SUMMARY: Notice is hereby given that NMFS has prepared a final environmental assessment (EA) under the National Environmental Policy Act (NEPA) describing the potential effects of Stockton East Water District's (District) proposed Calaveras River Habitat Conservation Plan (HCP). The Calaveras River HCP was prepared and submitted by the District and describes their ongoing operations and monitoring activities in the Calaveras River.

ADDRESSES: The incidental take permit, final environmental assessment, and other related documents are available on the NMFS West Coast Region website at: *https://www.fisheries.noaa.gov/action/calaveras-river-habitat-conservation-plan-and-environmental-assessment.*

FOR FURTHER INFORMATION CONTACT: Monica Gutierrez, Sacramento, CA, at phone number: (916) 930–3657, via fax: (916) 930–3629, or via email: *Monica.Gutierrez@noaa.gov.*

SUPPLEMENTARY INFORMATION:

ESA-Listed Species Covered in This Notice

Chinook salmon (*Oncorhynchus tshawytscha*): winter-run Chinook salmon, spring-run Chinook salmon, and fall/late fall-run Chinook salmon.

California Central Valley (CCV) steelhead (*O. mykiss*).

Background

The District is seeking coverage under section 10(a)(1)(B) of the Endangered Species Act (ESA) for their ongoing operations and monitoring program in the lower Calaveras River in California's Central Valley. The Calaveras River, a tributary to the San Joaquin River, serves as an important source of water for fish, agriculture, and municipal uses in Calaveras and San Joaquin counties. The District manages the water resources within the Calaveras River during non-flood control periods for their respective constituents. The Calaveras River provides valuable habitat for CCV steelhead and Chinook salmon. The District's operations may result in impacts to listed species and their habitat within the Calaveras River. Therefore, the District is required to work collaboratively with NMFS to minimize these impacts through implementation of the HCP upon issuance of the Section 10(a)(1)(B) Permit.

On September 30, 2019, a notice of receipt was published in the **Federal Register** (84 FR 51518) that a request for a permit for the incidental take of winter-run Chinook salmon, spring-run Chinook salmon, fall/late fall-run Chinook salmon, and CCV steelhead associated with the activities as described in the Calaveras River HCP, had been submitted by the District. In addition, the draft EA was available for 45-day public comment period. NMFS received several comments and these comments were addressed as changes to the final EA or as a response in the final EA appendix. The requested permit has been issued under the authority of the Endangered Species Act of 1973. This permit authorizes the incidental take of listed species as set forth in the HCP and the permit for a 50-year period.

Authority

Section 9 of the ESA and Federal regulations prohibit the 'taking' of a species listed as endangered or threatened. The ESA defines ''take'' to mean harass, harm, pursue, hunt, shoot, wound, kill, trap, capture, or collect, or to attempt to engage in any such conduct. NMFS may issue permits, under limited circumstances to take listed species incidental to, and not the purpose of, otherwise lawful activities. Section 10(a)(1)(B) of the ESA provides for authorizing incidental take of listed species. NMFS regulations governing permits for threatened and endangered species are promulgated at 50 CFR 222.307.

Dated: September 8, 2020.

Angela Somma,

Chief, Endangered Species Division, Office of Protected Resources, National Marine Fisheries Service.

[FR Doc. 2020–20111 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[RTID 0648–XA482]

Pacific Fishery Management Council; Public Meeting

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of public meeting.

SUMMARY: The Pacific Fishery Management Council's (Pacific Council) Climate and Communities Core Team (CCCT) will hold an online meeting, which is open to the public.

DATES: The online meeting will be held Tuesday, September 29, 2020, from 3 p.m. to 4:30 p.m., Pacific Daylight Time or until business is concluded.

ADDRESSES: This meeting will be held online. Specific meeting information, including directions on how to join the meeting and system requirements will be provided in the meeting announcement on the Pacific Council's website (see *www.pcouncil.org*). You may send an email to Mr. Kris Kleinschmidt (*kris.kleinschmidt@noaa.gov*) or contact him at (503) 820–2280, extension 412 for technical assistance.

Council address: Pacific Fishery Management Council, 7700 NE Ambassador Place, Suite 101, Portland, OR 97220–1384.

FOR FURTHER INFORMATION CONTACT: Kit Dahl, Staff Officer, Pacific Council; telephone: 503–820–2422.

SUPPLEMENTARY INFORMATION: The purpose of this CCCT online meeting is to plan a series of ''implications workshops'' as part of the climate change scenario planning process, which is a component of the Fishery Ecosystem Plan Climate and Communities Initiative. A series of four regionally-focused online workshops have been proposed that would occur in fall/winter of 2020/21. A proposal describing the workshops is available on the Council's website (*www.pcouncil.org*) as part of the briefing materials for the Council's September 8–18 meeting, see Agenda Item F.1, Attachment 2.

Although non-emergency issues not contained in the meeting agenda may be discussed, those issues may not be the subject of formal action during this meeting. Action will be restricted to those issues specifically listed in this document and any issues arising after publication of this document that require emergency action under section 305(c) of the Magnuson-Stevens Fishery Conservation and Management Act, provided the public has been notified of the intent to take final action to address the emergency.

Special Accommodations

Requests for sign language interpretation or other auxiliary aids should be directed to Mr. Kris Kleinschmidt (*kris.kleinschmidt@noaa.gov;* (503) 820–2412) at least 10 days prior to the meeting date.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: September 9, 2020.

Tracey L. Thompson,

Acting Deputy Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–20199 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[RTID 0648–XA473]

North Pacific Fishery Management Council; Public Meeting

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of a public meeting.

SUMMARY: The North Pacific Fishery Management Council's (Council) Scientific and Statistical Committee (SSC) will meet via webconference.

DATES: The Council's SSC will begin at 8 a.m. on Monday, September 28, 2020 and continue through Friday, October 2, 2020, Alaska Time.

ADDRESSES: The meeting will be a webconference. Join online through the link at *https://meetings.npfmc.org/Meeting/Details/1566.*

Council address: North Pacific Fishery Management Council, 1007 W 3rd Ave., Anchorage, AK 99501–2252; telephone: (907) 271–2809. Instructions for attending the meeting via webconference are given under Connection Information, below.

FOR FURTHER INFORMATION CONTACT: Diana Evans, Council staff; email: *diana.evans@noaa.gov;* telephone: (907) 271–2809. For technical support please contact our administrative staff, email: *npfmc.admin@noaa.gov.*

SUPPLEMENTARY INFORMATION:

Agenda

Monday, September 28, 2020 Through Friday, October 2, 2020

The SSC agenda will include the following issues:

(1) BSAI Crab 4 stocks—Final Specifications, Crab Plan Team Report
(2) BSAI and GOA Groundfish Harvest—Proposed Specifications, PT Reports
(3) Cook Inlet Salmon FMP—Intial Review
(4) BSAI Halibut ABM—Initial Review
(5) Survey Planning—AFSC Report

In addition to providing ongoing scientific advice for fishery management decisions, the SSC functions as the Council's primary peer review panel for scientific information, as described by the Magnuson-Stevens Act section 302(g)(1)(e), and the National Standard 2 guidelines (78 FR 43066). The peer review process is also deemed to satisfy the requirements of the Information Quality Act, including the OMB Peer

Connection Information

You can attend the meeting online using a computer, tablet, or smart phone; or by phone only. Connection information will be posted online at: *https://meetings.npfmc.org/Meeting/Details/1566.* For technical support please contact our administrative staff, email: *npfmc.admin@noaa.gov.*

Public Comment

Public comment letters will be accepted and should be submitted electronically to: *https://meetings.npfmc.org/Meeting/Details/1566.* The Council strongly encourages written public comment for this meeting, to avoid any potential for technical difficulties to compromise oral testimony. The deadline for written comments is September 25, 2020, at 5 p.m. Alaska Time.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: September 9, 2020.

Tracey L. Thompson,

Acting Deputy Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–20205 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[RTID 0648–XA432]

Pacific Fishery Management Council; Public Meeting

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of public meeting.

SUMMARY: The Pacific Fishery Management Council's (Pacific Council) Ad Hoc Southern Resident Killer Whale (SRKW) Workgroup (Workgroup) will host an online meeting over a two-day period that is open to the public.

DATES: The online meeting will be held Tuesday and Wednesday, September 29–30, 2020, starting at 9 a.m. (Pacific Daylight Time) and ending at 5 p.m. daily, or until business for the day is complete.

ADDRESSES: This meeting will be held online. Specific meeting information, including directions on how to join the meeting and system requirements will be provided in the meeting announcement on the Pacific Council's website (see *www.pcouncil.org*). You may send an email to Mr. Kris Kleinschmidt (*kris.kleinschmidt@noaa.gov*) or contact him at (503) 820–2412 for technical assistance.

Council address: Pacific Fishery Management Council, 7700 NE Ambassador Place, Suite 101, Portland, OR 97220–1384.

FOR FURTHER INFORMATION CONTACT: Ms. Robin Ehlke, Staff Officer, Pacific Council; telephone: (503) 820–2410.

SUPPLEMENTARY INFORMATION: The purpose of the meeting will be to continue to discuss any associated modeling and analysis needed to develop potential alternatives for salmon management/conservation measures for Pacific Council consideration. The Workgroup may also discuss and prepare for future Workgroup meetings and future meetings with the Pacific Council and its advisory bodies. Members of the Salmon Advisory Subpanel will be invited to attend. This is a public meeting and not a public hearing. Public comments will be taken at the discretion of the Workgroup co-chairs as time allows.

Although non-emergency issues not contained in the meeting agenda may be discussed, those issues may not be the subject of formal action during this meeting. Action will be restricted to those issues specifically listed in this document and any issues arising after publication of this document that require emergency action under section 305(c) of the Magnuson-Stevens Fishery Conservation and Management Act, provided the public has been notified of the intent to take final action to address the emergency.

Special Accommodations

Requests for sign language interpretation or other auxiliary aids should be directed to Mr. Kris Kleinschmidt (*kris.kleinschmidt@noaa.gov;* (503) 820–2412) at least 10 days prior to the meeting date.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: September 9, 2020.

Tracey L. Thompson,

Acting Deputy Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–20197 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[RTID 0648–XA447]

Gulf of Mexico Fishery Management Council; Public Meeting

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of a public meeting.

SUMMARY: The Gulf of Mexico Fishery Management Council (Council) will hold a three-day webinar meeting via webinar to consider actions affecting the Gulf of Mexico fisheries in the exclusive economic zone (EEZ).

DATES: The webinar will convene Monday, September 28, 2020 through Wednesday, September 30, 2020; 9 a.m. until 4 p.m. EDT.

ADDRESSES: The meeting will take place via webinar; you may register for the meeting at *www.gulfcouncil.org.*

Council address: Gulf of Mexico Fishery Management Council, 4107 W. Spruce Street, Suite 200, Tampa, FL 33607; telephone: (813) 348–1630.

FOR FURTHER INFORMATION CONTACT: Dr. Carrie Simmons, Executive Director, Gulf of Mexico Fishery Management Council; telephone: (813) 348–1630.

SUPPLEMENTARY INFORMATION:

Agenda

Monday, September 28, 2020; 9 a.m.–9:30 a.m.

The meeting will begin in a CLOSED SESSION of the FULL COUNCIL to make final selection of members to the Coastal Migratory Pelagics and Red Drum Advisory Panels.

Monday, September 28, 2020; 9:45 a.m.–4 p.m.

The meeting will open to the general public mid-morning beginning with the Administrative/Budget Committee review and approval of the Funded 2020 Budget. The Shrimp Committee will review and discuss the Analytical Requirement Program Updates and Reporting Options for Gulf Shrimp Fishery. The Mackerel Committee will receive an update on Coastal Migratory Pelagics Landings; and, review of SEDAR 28 Update: Gulf of Mexico Migratory Group Cobia Stock Assessment. The Sustainable Fisheries Committee will review Aquaculture Aspects of Executive Order 13921, and receive recommendations and public comments on Executive Order 13921; Draft letter on RESTAURANTs Act of 2020 (S. 4012); receive a presentation on Depredation by Marine Mammals; and review Public Hearing Draft Amendment Reef Fish 48/Red Drum 5: Status Determination Criteria and Optimum Yield for Reef Fish and Red Drum.

Tuesday, September 29, 2020; 9 a.m.–4 p.m.

The Reef Fish Committee will review the Reef Fish Landings; discuss the Fishing Industry Impacts Due to COVID–19 and Potential Emergency Rule Requests; and, receive status of Gulf State Recreational Data Collection Programs and 2020 Red Snapper Seasons. The Committee will receive an update from the Marine Recreational Information Program (MRIP) Fishing Effort Survey Calibration Workshop; and, receive a meeting summary from the August 5, 2020 MRIP Red Snapper State Data Calibration Meeting and SSC recommendations.

The Gulf of Mexico Fishery Management Council and National Marine Fisheries Service (NMFS) will hold a Question and Answer session immediately following the Reef Fish Committee.

Wednesday, September 30, 2020; 9 a.m.–4 p.m.

Full Council will convene with a Call to Order, Announcements, and Introductions; Induction of New Council Members; Adoption of Agenda and Approval of Minutes. The Council will hold public comment testimony beginning at approximately 9:30 a.m. until 11 a.m. on Comments on Executive Order 13921; and, open testimony on other fishery issues or concerns. Public comment may begin earlier than 9:30 a.m. EDT but will not conclude before that time. Persons wishing to give public testimony must register on the Council website before the start of the public comment period at 9:30 a.m. EDT.

The Council will continue to receive committee reports from Administrative/Budget, Shrimp, Sustainable Fisheries, Mackerel, and Reef Fish Committees. The Council will announce the Coastal Migratory Pelagics and Red Drum Advisory Panel appointments.

The Council will discuss Other Business item 5th Court Aquaculture Appellate Decision; and, hold an election for Council Chair and Vice-Chair.

—Meeting Adjourns

The meeting will be broadcast via webinar. You may register for the webinar by visiting *www.gulfcouncil.org* and clicking on the Council meeting on the calendar.

The timing and order in which agenda items are addressed may change as required to effectively address the issue, and the latest version along with other meeting materials will be posted on the website as they become available.

Although other non-emergency issues not contained in this agenda may come before this group for discussion, in accordance with the Magnuson-Stevens Fishery Conservation and Management Act (Magnuson-Stevens Act), those issues may not be the subject of formal action during this meeting. Actions will be restricted to those issues specifically listed in this notice and any issues arising after publication of this notice that require emergency action under Section 305(c) of the Magnuson-Stevens Act, provided that the public has been notified of the Council's intent to take final action to address the emergency.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: September 9, 2020.

Tracey L. Thompson,

Acting Deputy Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–20198 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

[RTID 0648–XA470]

Caribbean Fishery Management Council; Public Meeting

AGENCY: National Marine Fisheries Service (NMFS), National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of a public meeting.

SUMMARY: The Caribbean Fishery Management Council's (Council) Outreach and Education Advisory Panel (OEAP) will hold a public virtual meeting to address the items contained in the tentative agenda included in the **SUPPLEMENTARY INFORMATION.**

DATES: The OEAP public virtual meeting will be held on September 30, 2020, from 10 a.m. to 3 p.m., Eastern Day Time.

ADDRESSES: You may join the OEAP public virtual meeting (via GoToMeeting) from a computer, tablet or smartphone by entering the following address: *https://global.gotomeeting.com/join/431849525.*

You can also dial in using your phone. United States: +1 (646) 749–3112, Access Code: 431–849–525.

Get the app now and be ready when the first meeting starts: *https://global.gotomeeting.com/install/431849525.*

In case GoToMeeting fails: Via Google Meets, in case GTM fails: *https://meet.google.com/qjf-rhak-ayy.*

FOR FURTHER INFORMATION CONTACT: Miguel Rolón, Executive Director, Caribbean Fishery Management Council, 270 Muñoz Rivera Avenue, Suite 401, San Juan, Puerto Rico 00918–1903, telephone: (787) 398–3717.

SUPPLEMENTARY INFORMATION: The following items included in the tentative agenda will be discussed:

Wednesday, September 30, 2020, 10 a.m.–3 p.m.

10 a.m.—11 a.m.

—Call to Order
—Adoption of Agenda
—Needs for Outreach and Education on Marine Reserves

11 a.m.–11:10 a.m.

—Break

11:10 a.m.–12 p.m.

—Possible Outreach and Education Products

12 p.m.–1 p.m.

—Lunch

1 p.m.–2 p.m.

—Outreach & Education Products on Critical Habitats

2 p.m.–2:10 p.m.

—Break

2:10 p.m.–3 p.m.

—How can OEAP members contribute to dissemination of O & E products?
—Other Business

The order of business may be adjusted as necessary to accommodate the completion of agenda items. The meeting will begin on September 30, 2020, at 10 a.m. EST, and will end on September 30, 2020, at 3 p.m. EST. Other than the start time, interested parties should be aware that discussions may start earlier or later than indicated, at the discretion of the Chair. In addition, the meeting may be completed prior to the date established in this notice.

Special Accommodations

For any additional information on this public virtual meeting, please contact Diana Martino, Caribbean Fishery Management Council, 270 Muñoz Rivera Avenue, Suite 401, San Juan, Puerto Rico, 00918–1903, telephone: (787) 226–8849.

Authority: 16 U.S.C. 1801 *et seq.*

Dated: September 9, 2020.

Tracey L. Thompson,

Acting Deputy Director, Office of Sustainable Fisheries, National Marine Fisheries Service.

[FR Doc. 2020–20207 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration

Agency Information Collection Activities; Submission to the Office of Management and Budget (OMB) for Review and Approval; Comment Request; Pacific Islands Region Permit Family of Forms

AGENCY: National Oceanic and Atmospheric Administration (NOAA), Commerce.

ACTION: Notice of information collection, request for comments.

SUMMARY: The Department of Commerce, in accordance with the Paperwork Reduction Act of 1995 (PRA), invites the general public and other Federal agencies to comment on proposed and continuing information collections, which helps us assess the impact of our information collection requirements and minimize the public's reporting burden. The purpose of this notice is to allow for 60 days of public comment preceding submission of the collection to OMB.

DATES: To ensure consideration, comments regarding this proposed information collection must be received on or before November 13, 2020.

ADDRESSES: Interested persons are invited to submit written comments to Adrienne Thomas, NOAA PRA Officer, at *Adrienne.thomas@noaa.gov.* Please reference OMB Control Number 0648–0490 in the subject line of your comments. Do not submit Confidential Business Information or otherwise sensitive or protected information.

FOR FURTHER INFORMATION CONTACT: Requests for additional information or specific questions related to collection activities should be directed to Walter Ikehara, Fishery Information Specialist, National Marine Fisheries Service, Pacific Islands Region, 1845 Wasp Blvd., Bldg. 176, Honolulu, HI 96818, (808) 725–5175, *walter.ikehara@noaa.gov.*

SUPPLEMENTARY INFORMATION:

I. Abstract

This request is for an extension, with a minor technical revision, of a currently approved information collection.

The *Magnuson-Stevens Fishery Conservation and Management Act* established the Western Pacific Fishery Management Council (Council), to develop fishery ecosystem plans (FEP) for fisheries in the United States (U.S.) exclusive economic zone (EEZ) and high seas of the Pacific Islands region. These plans, if approved by the Secretary of Commerce, are implemented in Federal regulations by the National Oceanic and Atmospheric Administration's (NOAA) National Marine Fisheries Service (NMFS) and enforced by NOAA's Office of Law Enforcement (OLE) and the U.S. Coast Guard (USCG), in cooperation with state and territorial agencies. FEPs regulate fishing to prevent overfishing and to ensure the long-term productivity and social and economic benefit of the resources.

Regulations at 50 CFR 665, Subpart F, require that a vessel used to fish with longline gear for western Pacific pelagic management unit species (PMUS), land or transship longline caught PMUS, or receive longline caught PMUS from a longline vessel, within the Exclusive Economic Zone (EEZ) or management subarea around U.S. islands in the central and western Pacific must be registered to a valid Federal fishing permit. The regulations also require that a vessel used to fish with squid jig gear for pelagic squid species listed in the western Pacific PMUS within the EEZ or management subareas around U.S. islands in the central and western Pacific, or fish with troll and handline gear for PMUS in allowed locations within the EEZ around each of the Pacific Remote Island Areas (PRIA), must be registered to a valid Federal fishing permit.

Regulations at 50 CFR parts 665, Subparts D and E, require that the owner of a vessel used to fish for, land, or transship bottomfish management unit species (BMUS) using a large vessel (50 ft or longer) in the Guam management subarea, fish commercially for BMUS in the Commonwealth of the Northern Mariana Islands management subarea, or fish for BMUS in allowed locations within the EEZ around each of the PRIA, must register it to a valid Federal fishing permit.

Regulations at 50 CFR parts 665, Subparts B, C, D, and E, require that the owner of a vessel used to fish for, land, or transship crustacean management unit species (CMUS) in the EEZs or management subareas around American Samoa, Hawaii, Guam, Northern Mariana Islands, or in allowed locations within the EEZ around each of the PRIA, must register it to a valid Federal fishing permit. The regulations also require that a vessel used to fish for precious corals within the EEZ or management subarea around U.S. islands in the central and western Pacific must be registered to a valid Federal fishing permit for a specific precious coral permit area.

This collection of information is needed for permit issuance, to identify actual or potential participants in the fishery, determine qualifications for permits, and to help measure the impacts of management controls on the participants in the fishery. The permit program is also an effective tool in the enforcement of fishery regulations and facilitates communication between NMFS and fishermen.

This collection will be revised to remove the instruction to mail applications to NMFS as the office is currently unable to accept or process mail. Individuals will be able to submit applications electronically either through secure email or by applying directly through the National Permit System for the Hawaii longline limited entry permit.

II. Method of Collection

Respondents may submit applications and required documents via secure email, or via online application systems where implemented.

III. Data

OMB Control Number: 0648–0490.

Form Number(s): None.

Type of Review: Regular submission (Revision and extension of an existing collection).

Affected Public: Business or other for-profit organizations; individuals or households; not-for-profit institutions; state, local, or tribal government; Federal government.

Estimated Number of Respondents: 276

Estimated Time per Response: Hawaii longline limited entry permit: Renew via secure email—30 min; renew online—15 min; transfer—1 hour; apply for closed area exemption or permit appeal—2 hr. American Samoa longline limited entry permit: renew or apply for additional permit via secure email—45 min; transfer—1 hour 15 min; permit appeal—2 hours. All other permits: apply via secure email—30 min; apply online—15 min.

Estimated Total Annual Burden Hours: 131.5

Estimated Total Annual Cost to Public: $12,650

Respondent's Obligation: Mandatory

Legal Authority: 50 CFR 665

IV. Request for Comments

We are soliciting public comments to permit the Department to: (a) Evaluate whether the proposed information collection is necessary for the proper functions of the Department, including whether the information will have practical utility; (b) Evaluate the accuracy of our estimate of the time and cost burden for this proposed collection, including the validity of the methodology and assumptions used; (c) Evaluate ways to enhance the quality, utility, and clarity of the information to be collected; and (d) Minimize the reporting burden on those who are to respond, including the use of automated collection techniques or other forms of information technology.

Comments that you submit in response to this notice are a matter of public record. We will include or summarize each comment in our request to OMB to approve this Information Collection Request. Before including your address, phone number, email address, or other personal identifying information in your comment, you should be aware that your entire comment—including your personal identifying information—may be made publicly available at any time. While you may ask us in your comment to withhold your personal identifying information from public review, we cannot guarantee that we will be able to do so.

Sheleen Dumas,

Department PRA Clearance Officer, Office of the Chief Information Officer, Commerce Department.

[FR Doc. 2020–20201 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–22–P

DEPARTMENT OF COMMERCE

National Oceanic and Atmospheric Administration (NOAA)

Ocean Exploration Advisory Board (OEAB); Ocean Exploration Advisory Board; Meeting

AGENCY: Office of Ocean Exploration and Research (OER), National Oceanic and Atmospheric Administration (NOAA), Department of Commerce (DOC).

ACTION: Notice of public meeting.

SUMMARY: This notice sets forth the schedule and proposed agenda for a meeting of the Ocean Exploration Advisory Board (OEAB). OEAB members will discuss and provide advice on Federal ocean exploration programs, with a particular emphasis on

the topics identified in the section on Matters to Be Considered.

DATES: The announced meeting is scheduled for Thursday, October 1, 2020, from 1:00 p.m. to 5:00 p.m. EDT and Friday, October 2, 2020, from 1:00 p.m. to 5:00 p.m. EDT.

ADDRESSES: This will be a virtual meeting. Information about how to participate will be posted to the OEAB website at *http://oeab.noaa.gov.*

FOR FURTHER INFORMATION CONTACT: Mr. David McKinnie, Designated Federal Officer, Ocean Exploration Advisory Board, National Oceanic and Atmospheric Administration, 7600 Sand Point Way NE, Seattle, WA 98115, (206) 526–6950.

SUPPLEMENTARY INFORMATION: NOAA established the OEAB under the Federal Advisory Committee Act (FACA) and legislation that gives the agency statutory authority to operate an ocean exploration program and to coordinate a national program of ocean exploration. The OEAB advises NOAA leadership on strategic planning, exploration priorities, competitive ocean exploration grant programs, and other matters as the NOAA Administrator requests.

OEAB members represent government agencies, the private sector, academic institutions, and not-for-profit institutions involved in all facets of ocean exploration—from advanced technology to citizen exploration.

In addition to advising NOAA leadership, NOAA expects the OEAB to help to define and develop a national program of ocean exploration—a network of stakeholders and partnerships advancing national priorities for ocean exploration.

Matters to be Considered: The OEAB will discuss the following topics: (1) NOAA Office of Ocean Exploration and Research program review and other updates; (2) the National Strategy for Mapping, Exploring, and Characterizing the United States Exclusive Economic Zone; (3) ocean exploration partnerships; (4) national ocean exploration priorities in the Pacific; and (5) other matters as described in the agenda. The agenda and other meeting materials will be made available on the OEAB website at *http://oeab.noaa.gov.*

Status: The meeting will be open to the public with a 15-minute public comment period on Friday, October 2, 2020, from 3:00 p.m. to 3:15 p.m. EDT (please check the final agenda on the OEAB website to confirm the time). The public may listen to the meeting and provide comments during the public comment period via teleconference. Participation information will be on the meeting agenda on the OEAB website.

The OEAB expects that public statements at its meetings will not be repetitive of previously submitted verbal or written statements. In general, each individual or group making a verbal presentation will be limited to three minutes. The Designated Federal Officer must receive written comments by September 28, 2020, to provide sufficient time for OEAB review. Written comments received after September 28, 2020, will be distributed to the OEAB but may not be reviewed prior to the meeting date.

Special Accomodations: Requests for sign language interpretation or other auxiliary aids should be directed to the Designated Federal Officer by September 28, 2020.

Dated: September 8, 2020.

David Holst,

Director Chief Financial Officer/CAO, Office of Oceanic and Atmospheric Research, National Oceanic and Atmospheric Administration.

[FR Doc. 2020–20117 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–KA–P

DEPARTMENT OF COMMERCE

National Telecommunications and Information Administration

Agency Information Collection Activities; Submission to the Office of Management and Budget (OMB) for Review and Approval; Comment Request; NTIA internet Use Survey

The Department of Commerce will submit the following information collection request to the Office of Management and Budget (OMB) for review and clearance in accordance with the Paperwork Reduction Act of 1995, on or after the date of publication of this notice. We invite the general public and other Federal agencies to comment on proposed, and continuing information collections, which helps us assess the impact of our information collection requirements and minimize the public's reporting burden. Public comments were previously requested via the **Federal Register** on July 7, 2020 during a 60-day comment period. This notice allows for an additional 30 days for public comments.

Agency: National Telecommunications and Information Administration.

Title: NTIA internet Use Survey.

OMB Control Number: 0660–0021.

Form Number(s): None.

Type of Request: Regular submission (Extension of a current information collection).

Number of Respondents: 54,000 households.

Estimated Time per Response: 10 minutes.

Burden Hours: 9,000.

Needs and Uses: Data from the NTIA internet Use Survey will be used to help inform federal policies related to digital inclusion and other internet-related issues. NTIA will use the data both in relevant publications and to help inform policymakers. Additionally, a public use dataset that protects respondent confidentiality will be created by the Census Bureau and made available by both agencies for use by researchers and other members of the public.

Affected Public: Individuals and households.

Frequency: Biennial.

Respondent's Obligation: Voluntary.

Legal Authority: 47 U.S.C. 902(b)(2)(M), (P).

This information collection request may be viewed at *www.reginfo.gov.* Follow the instructions to view the Department of Commerce collections currently under review by OMB.

Written comments and recommendations for the proposed information collection should be submitted within 30 days of the publication of this notice on the following website *www.reginfo.gov/public/do/PRAMain.* Find this particular information collection by selecting ''Currently under 30-day Review—Open for Public Comments'' or by using the search function and entering either the title of the collection or the OMB Control Number 0660–0021.

Sheleen Dumas,

Department PRA Clearance Officer, Office of the Chief Information Officer, Commerce Department.

[FR Doc. 2020–20204 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–60–P

DEPARTMENT OF COMMERCE

United States Patent and Trademark Office

[Docket No. PTO–C–2020–0038]

Performance Review Board

AGENCY: United States Patent and Trademark Office, Commerce.

ACTION: Notice.

SUMMARY: In conformance with the Civil Service Reform Act of 1978, the United States Patent and Trademark Office (USPTO) announces the appointment of persons to serve as members of its Performance Review Board (PRB). The PRB reviews and makes recommendations concerning proposed

performance appraisals, ratings, bonuses, pay adjustments, and other appropriate personnel actions for incumbents of Senior Level and Senior Executive Service positions within USPTO.

ADDRESSES: Office of Human Resources, United States Patent and Trademark Office, P.O. Box 1450, Alexandria, VA 22313–1450.

FOR FURTHER INFORMATION CONTACT: Anne T. Mendez, Director, Human Capital Management, at 571–272–6173.

SUPPLEMENTARY INFORMATION: The membership of the USPTO's PRB is as follows:

Laura A. Peter, Chair, Deputy Under Secretary of Commerce for Intellectual Property and Deputy Director of the USPTO
Frederick W. Steckler, Vice Chair, Chief Administrative Officer, USPTO
Andrew H. Hirshfeld, Commissioner for Patents, USPTO
David S. Gooder, Commissioner for Trademarks, USPTO
Dennis J. Hoffman, Chief Financial Officer, USPTO
Henry J. Holcombe, Chief Information Officer, USPTO
Nicholas T. Matich IV, Acting General Counsel, USPTO
Shira Perlmutter, Chief Policy Officer and Director for International Affairs, USPTO Alternates
Meryl L. Hershkowitz, Deputy Commissioner for Trademark Operations, USPTO
Andrew I. Faile, Deputy Commissioner for Patents, USPTO

Dated: September 3, 2020.

Andrei Iancu,

Under Secretary of Commerce for Intellectual Property and Director of the United States Patent and Trademark Office.

[FR Doc. 2020–20181 Filed 9–11–20; 8:45 am]

BILLING CODE 3510–20–P

CONSUMER PRODUCT SAFETY COMMISSION

[Docket No. CPSC–2010–0056]

Agency Information Collection Activities; Proposed Extension of Approval of Information Collection; Comment Request—Safety Standard for Bicycle Helmets

AGENCY: Consumer Product Safety Commission.

ACTION: Notice.

SUMMARY: As required by the Paperwork Reduction Act of 1995, the Consumer Product Safety Commission (CPSC or Commission) requests comments on a proposed extension of approval for a collection of information relating to the Safety Standard for Bicycle Helmets. The Office of Management and Budget (OMB) previously approved the collection of information under control number 3041–0127. OMB's most recent extension of approval will expire on December 31, 2020. The Commission will consider all comments received in response to this notice before requesting an extension of approval of this collection of information from OMB.

DATES: Submit written or electronic comments on the collection of information by November 13, 2020.

ADDRESSES: You may submit comments, identified by Docket No. CPSC–2010–0056, by any of the following methods:

Electronic Submissions: Submit electronic comments to the Federal eRulemaking Portal at: *https://www.regulations.gov.* Follow the instructions for submitting comments. The CPSC does not accept comments submitted by electronic mail (email), except through *https://www.regulations.gov.* The CPSC encourages you to submit electronic comments by using the Federal eRulemaking Portal, as described above.

Mail/Hand Delivery/Courier Written Submissions: Submit comments by mail/hand delivery/courier to: Division of the Secretariat, Consumer Product Safety Commission, Room 820, 4330 East West Highway, Bethesda, MD 20814; telephone (301) 504–7479.

Instructions: All submissions received must include the agency name and docket number for this notice. All comments received may be posted without change, including any personal identifiers, contact information, or other personal information provided, to: *https://www.regulations.gov.* Do not submit electronically confidential business information, trade secret information, or other sensitive or protected information that you do not want to be available to the public. If you wish to submit such information, please submit it according to the instructions for written submissions.

Docket: For access to the docket to read background documents or comments received, go to: *https://www.regulations.gov,* and insert the docket number, CPSC–2010–0056, into the ''Search'' box, and follow the prompts.

FOR FURTHER INFORMATION CONTACT: Cynthia Gillham, Consumer Product Safety Commission, 4330 East West Highway, Bethesda, MD 20814; (301) 504–7791, or by email to: *cgillham@cpsc.gov.*

SUPPLEMENTARY INFORMATION: CPSC seeks to renew the following collection of information:

Title: Safety Standard for Bicycle Helmets.

OMB Number: 3041–0127.

Type of Review: Renewal of collection.

Frequency of Response: On occasion.

Affected Public: Manufacturers and importers of bicycle helmets.

Estimated Number of Respondents: 38 manufacturers and importers will maintain test records of an estimated 200 models total annually, including older models and new models. Testing on bicycle helmets must be conducted for each new production lot and the test records must be maintained for 3 years.

Estimated Time per Response: 200 hours/model to test 40 new models (including new prototypes) and an estimated 100 hours/model to test new production lots of 160 older models. Additionally, manufacturers and importers may require 4 hours annually per model for recordkeeping for approximately 200 models.

Total Estimated Annual Burden: 24,800 hours (24,000 hours for testing and 800 hours for recordkeeping).

General Description of Collection: In 1998, the Commission issued a safety standard for bicycle helmets (16 CFR part 1203). The standard includes requirements for labeling and instructions. The standard also requires that manufacturers and importers of bicycle helmets subject to the standard issue certificates of compliance based on a reasonable testing program. Every person issuing certificates of compliance must maintain certain records. Respondents must comply with the requirements in 16 CFR part 1203 for labeling and instructions, testing, certification, and recordkeeping.

Request for Comments

The Commission solicits written comments from all interested persons about the proposed collection of information. The Commission specifically solicits information relevant to the following topics:

- Whether the collection of information described above is necessary for the proper performance of the Commission's functions, including whether the information would have practical utility;
- Whether the estimated burden of the proposed collection of information is accurate;
- Whether the quality, utility, and clarity of the information to be collected could be enhanced; and
- Whether the burden imposed by the collection of information could be

minimized by use of automated, electronic or other technological collection techniques, or other forms of information technology.

Alberta E. Mills,

Secretary, Consumer Product Safety Commission.

[FR Doc. 2020–20196 Filed 9–11–20; 8:45 am]

BILLING CODE 6355–01–P

DEPARTMENT OF DEFENSE

Office of the Secretary

[Docket ID DoD–2020–OS–0072]

Proposed Collection; Comment Request

AGENCY: Defense Counterintelligence and Security Agency (DCSA), DoD.

ACTION: Information collection notice.

SUMMARY: In compliance with the *Paperwork Reduction Act of 1995,* the Defense Counterintelligence and Security Agency announces a proposed public information collection and seeks public comment on the provisions thereof. Comments are invited on: whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility; the accuracy of the agency'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 information collection on respondents, including through the use of automated collection techniques or other forms of information technology.

DATES: Consideration will be given to all comments received by November 13, 2020.

ADDRESSES: You may submit comments, identified by docket number and title, by any of the following methods:

Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.

Mail: DoD cannot receive written comments at this time due to the COVID–19 pandemic. Comments should be sent electronically to the docket listed above.

Instructions: All submissions received must include the agency name, docket number and title for this **Federal Register** document. The general policy for comments and other submissions from members of the public is to make these submissions available for public viewing on the internet at *http://www.regulations.gov* as they are received without change, including any personal identifiers or contact information.

FOR FURTHER INFORMATION CONTACT: To request more information on this proposed information collection or to obtain a copy of the proposal and associated collection instruments, please write to Defense Counterintelligence and Security Agency, ATTN: Ms. Michele DeMarion, 1137 Branchton Road, Boyers, PA 16018, or call 724–794–5612 ext. 5274.

SUPPLEMENTARY INFORMATION:

Title; Associated Form; and OMB Number: Standard Form 87 Fingerprint Charts; SF 87; OMB Control Number 0705–0002.

Needs and Uses: The SF 87 is a fingerprint card, which is utilized to conduct a national criminal history check, which is a component of the background investigation. The SF 87 is completed by applicants who are under consideration for Federal employment; by Federal employees, to determine whether they should be retained in such employment; by individuals being considered to perform work for the Federal Government under a Government contract or to continue such work; and by persons seeking long-term access to Federal facilities and systems. The SF 87 fingerprint chart is used in background investigations to help establish facts required to determine, for example, whether the subject of the investigation should be adjudicated to be eligible for logical and physical access to Government facilities and systems; suitable or fit for Federal employment; fit to perform work on behalf of the Federal Government under a Government contract; eligible to hold a position that is sensitive for national security reasons; or eligible for access to classified information. The SF 87 form is utilized only when a hardcopy fingerprint chart must be obtained, as opposed to the electronic collection of fingerprints.

Affected Public: Individuals or Households.

Annual Burden Hours: 4,317.

Number of Respondents: 51,800.

Responses per Respondent: 1.

Annual Responses: 51,800.

Average Burden per Response: 5 minutes.

Frequency: On occasion.

Dated: September 8, 2020.

Aaron T. Siegel,

Alternate OSD Federal Register Liaison Officer, Department of Defense.

[FR Doc. 2020–20146 Filed 9–11–20; 8:45 am]

BILLING CODE 5001–06–P

DEPARTMENT OF DEFENSE

Department of the Army

[Docket ID USA–2020–HQ–0007]

Submission for OMB Review; Comment Request

AGENCY: U.S. Army Corps of Engineers (USACE), Department of Defense (DoD).

ACTION: 30-day information collection notice.

SUMMARY: The DoD has submitted to OMB for clearance the following proposal for collection of information under the provisions of the Paperwork Reduction Act.

DATES: Consideration will be given to all comments received by October 14, 2020.

ADDRESSES: Written comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *www.reginfo.gov/public/do/PRAMain.* Find this particular information collection by selecting ''Currently under 30-day Review—Open for Public Comments'' or by using the search function.

FOR FURTHER INFORMATION CONTACT: Angela James, 571–372–7574, or *whs.mc-alex.esd.mbx.dd-dod-information-collections@mail.mil.*

SUPPLEMENTARY INFORMATION:

Title; Associated Form; and OMB Number: Silver Jackets Program Nomination and Awards; Eng Form 6128; OMB Control Number 0710–XXXX.

Type of Request: New.

Number of Respondents: 54.

Responses per Respondent: 2.

Annual Responses: 108.

Average Burden per Response: 15 minutes.

Annual Burden Hours: 27.

Needs and Uses: The information collection request is necessary to obtain input and feedback into the successes of various Silver Jackets State Teams deserving of recognition through annual awards. Because the program is a shared program, state partners need to have a role in selecting the teams deserving of annual recognition. The form provides a means of nominating teams for consideration and can be filled out by State government employees. State government employees are also asked to vote for the nominated team most deserving of recognition after the nomination phase is complete.

Affected Public: State, Local, or Tribal government.

Frequency: Annually.

Respondent's Obligation: Voluntary.

OMB Desk Officer: Mr. Vlad Dorjets.

You may also submit comments and recommendations, identified by Docket ID number and title, by the following method:

• *Federal eRulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.

Instructions: All submissions received must include the agency name, Docket ID number, and title for this **Federal Register** document. The general policy for comments and other submissions from members of the public is to make these submissions available for public viewing on the internet at *http://www.regulations.gov* as they are received without change, including any personal identifiers or contact information.

DOD Clearance Officer: Ms. Angela James.

Requests for copies of the information collection proposal should be sent to Ms. James at *whs.mc-alex.esd.mbx.dd-dod-information-collections@mail.mil.*

Dated: September 8, 2020.

Aaron T. Siegel,

Alternate OSD Federal Register Liaison Officer, Department of Defense.

[FR Doc. 2020–20145 Filed 9–11–20; 8:45 am]

BILLING CODE 5001–06–P

DEPARTMENT OF DEFENSE

Department of the Navy

[Docket ID USN–2020–HQ–0007]

Proposed Collection; Comment Request

AGENCY: Department of the Navy, DoD.

ACTION: Information collection notice.

SUMMARY: In compliance with the *Paperwork Reduction Act of 1995,* the United States Marine Corps announces a proposed public information collection and seeks public comment on the provisions thereof. Comments are invited on: Whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility; the accuracy of the agency'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 information collection on respondents, including through the use of automated collection techniques or other forms of information technology.

DATES: Consideration will be given to all comments received by November 13, 2020.

ADDRESSES: You may submit comments, identified by docket number and title, by any of the following methods:

Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.

Mail: DoD cannot receive written comments at this time due to the COVID–19 pandemic. Comments should be sent electronically to the docket listed above.

Instructions: All submissions received must include the agency name, docket number and title for this **Federal Register** document. The general policy for comments and other submissions from members of the public is to make these submissions available for public viewing on the internet at *http://www.regulations.gov* as they are received without change, including any personal identifiers or contact information.

FOR FURTHER INFORMATION CONTACT: To request more information on this proposed information collection or to obtain a copy of the proposal and associated collection instruments, please write to Office of the Department of the Navy Information Management Control Officer, 2000 Navy Pentagon, Rm. 4E563, Washington, DC 20350, Ms. Barbara Figueroa or call 703–614–7885.

SUPPLEMENTARY INFORMATION: *Title; Associated Form; and OMB Number:* USMC Children, Youth and Teen Programs (CYTP) Registration Packet; NAVMC Forms 11720, 1750/4 and 1750/5; OMB Control Number 0703–0068.

Needs and Uses: The information collected on these forms is used by MFP and Inclusion Action Team (IAT) professionals for purposes of patron registration, to determine the general health status of patrons participating in CYTP activities and if necessary the appropriate accommodations for the patron for full enjoyment of CYTP services, and provides consent for information to be exchanged between MFP personnel and other designated individuals or organizations about a patron participating in MFP.

Affected Public: Individuals or households; business or other for-profit.

Annual Burden Hours: 130,667.

Number of Respondents: 112,000.

Responses per Respondent: 1.

Annual Responses: 112,000.

Average Burden per Response: 70 minutes.

Frequency: Annually.

Dated: September 8, 2020.

Aaron T. Siegel,

Alternate OSD Federal Register Liaison Officer, Department of Defense.

[FR Doc. 2020–20148 Filed 9–11–20; 8:45 am]

BILLING CODE 5001–06–P

DEPARTMENT OF DEFENSE

Department of the Navy

[Docket ID USN–2020–HQ–0006]

Proposed Collection; Comment Request

AGENCY: Commander, Navy Installations Command, DoD.

ACTION: Information collection notice.

SUMMARY: In compliance with the *Paperwork Reduction Act of 1995,* the Commander, Navy Installations Command announces a proposed public information collection and seeks public comment on the provisions thereof. Comments are invited on: Whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility; the accuracy of the agency'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 information collection on respondents, including through the use of automated collection techniques or other forms of information technology.

DATES: Consideration will be given to all comments received by November 13, 2020.

ADDRESSES: You may submit comments, identified by docket number and title, by any of the following methods:

Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.

Mail: DoD cannot receive written comments at this time due to the COVID–19 pandemic. Comments should be sent electronically to the docket listed above.

Instructions: All submissions received must include the agency name, docket number and title for this **Federal Register** document. The general policy for comments and other submissions from members of the public is to make these submissions available for public viewing on the internet at *http://www.regulations.gov* as they are received without change, including any personal identifiers or contact information.

FOR FURTHER INFORMATION CONTACT: To request more information on this proposed information collection or to obtain a copy of the proposal and associated collection instruments, please write to Office of the Department of the Navy Information Management Control Officer, 2000 Navy Pentagon, Rm. 4E563, Washington, DC 20350, Ms. Barbara Figueroa or call 703–614–7885.

SUPPLEMENTARY INFORMATION: *Title; Associated Form; and OMB Number:* Law Enforcement Officers Safety Act (LEOSA) Credential Program; SECNAV Form 5580/1; OMB Control Number 0703–0067.

Needs and Uses: Department of the Navy and the U.S. Marine Corps are requesting Office of Management and Budget (OMB) approval of the information collection to verify and validate eligibility of separated and retired DON law enforcement officers to ship, transport, possess or receive Government-issued or private firearms or ammunition. This will also verify and validate eligibility of separated, and retired DON law enforcement officers to receive DON endorsed law enforcement credentials, to include Law Enforcement Officers Safety Act (LEOSA) credentials.

Affected Public: Individuals or households.

Annual Burden Hours: 450.

Number of Respondents: 900.

Responses per Respondent: 1.

Annual Responses: 900.

Average Burden per Response: 30 minutes.

Frequency: On occasion.

Dated: September 8, 2020.

Aaron T. Siegel,

Alternate OSD Federal Register Liaison Officer, Department of Defense.

[FR Doc. 2020–20147 Filed 9–11–20; 8:45 am]

BILLING CODE 5001–06–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Project No. 2305–123]

Sabine River Authority—LA & TX; Notice of Application Accepted for Filing and Soliciting Comments, Motions To Intervene, and Protests

Take notice that the following hydroelectric application has been filed with the Commission and is available for public inspection:

a. *Application Type:* Revised Shoreline Management Plan.

b. *Project No:* 2305–123.

c. *Date Filed:* July 29, 2020.

d. *Applicant:* Sabine River Authority—LA & TX.

e. *Name of Project:* Toledo Bend Hydroelectric Project.

f. *Location:* The Sabine River in Panola, Shelby, Sabine, and Newton counties in Texas and DeSoto, Sabine, and Vernon parishes in Louisiana.

g. *Filed Pursuant to:* Federal Power Act, 16 U.S.C. 791a–825r.

h. *Applicant Contact:* Jim Brown, Toledo Bend Project Joint Operation Compliance Officer, (409) 746–2192, *jbrown@sratx.org.*

i. *FERC Contact:* Mark Carter, (678) 245–3083, *mark.carter@ferc.gov.*

j. *Deadline for filing comments, motions to intervene, and protests:* October 8, 2020.

The Commission strongly encourages electronic filing. Please file comments, motions to intervene, and protests using the Commission's eFiling system at *http://www.ferc.gov/docs-filing/efiling.asp.* Commenters can submit brief comments up to 6,000 characters, without prior registration, using the eComment system at *http://www.ferc.gov/docs-filing/ecomment.asp.* You must include your name and contact information at the end of your comments. For assistance, please contact FERC Online Support at *FERCOnlineSupport@ferc.gov,* (866) 208–3676 (toll free), or (202) 502–8659 (TTY). In lieu of electronic filing, you may submit a paper copy. Submissions sent via the U.S. Postal Service must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 888 First Street NE, Room 1A, Washington, DC 20426. Submissions sent via any other carrier must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 12225 Wilkins Avenue, Rockville, Maryland 20852. The first page of any filing should include docket number P–2305–123. Comments emailed to Commission staff are not considered part of the Commission record.

The Commission's Rules of Practice and Procedure require all intervenors filing documents with the Commission to serve a copy of that document on each person whose name appears on the official service list for the project. Further, if an intervenor files comments or documents with the Commission relating to the merits of an issue that may affect the responsibilities of a particular resource agency, they must also serve a copy of the document on that resource agency.

k. *Description of Request:* As required by Article 411 of the August 29, 2014 license, Sabine River Authority—LA & TX (licensee) filed a revised shoreline management plan (SMP) for the project. The revised SMP is substantially similar to the original SMP approved in the 2014 license but includes a request for expanded permitting authority for certain activities (*e.g.,* fencing, maintenance dredging, energy and utility infrastructure without ground disturbing activities, private or public marinas that accommodate no more than 20 watercraft at one time, etc.) without the need for prior Commission approval.

l. *Locations of the Application:* In addition to publishing the full text of this document in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents of this document via the internet through the Commission's Home Page (*http://www.ferc.gov*) using the ''elibrary'' link. Enter the docket number excluding the last three digits in the document field to access the document. At this time, the Commission has suspended access to the Commission's Public Reference Room, due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID–19), issued by the President on March 13, 2020. For assistance, contact FERC at *FERCOnlineSupport@ferc.gov* or call toll-free, (886) 208–3673 or TYY, (202) 502–8659. Agencies may obtain copies of the application directly from the applicant.

m. Individuals desiring to be included on the Commission's mailing list should so indicate by writing to the Secretary of the Commission.

n. *Comments, Protests, or Motions to Intervene:* Anyone may submit comments, a protest, or a motion to intervene in accordance with the requirements of Rules of Practice and Procedure, 18 CFR 385.210, .211, .214, respectively. In determining the appropriate action to take, the Commission will consider all protests or other comments filed, but only those who file a motion to intervene in accordance with the Commission's Rules may become a party to the proceeding. Any comments, protests, or motions to intervene must be received on or before the specified comment date for the particular application.

o. *Filing and Service of Documents:* Any filing must (1) bear in all capital letters the title ''COMMENTS'', ''PROTEST'', or ''MOTION TO INTERVENE'' as applicable; (2) set forth in the heading the name of the applicant and the project number of the application to which the filing responds; (3) furnish the name, address, and telephone number of the person commenting, protesting or intervening; and (4) otherwise comply with the requirements of 18 CFR 385.2001 through 385.2005. All comments, motions to intervene, or protests must set forth their evidentiary basis. Any filing made by an intervenor must be accompanied by proof of service on all persons listed in the service list prepared by the Commission in this proceeding, in accordance with 18 CFR 385.2010.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20165 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Project No. 2955–011]

City of Watervliet, NY; Notice Soliciting Scoping Comments

Take notice that the following hydroelectric application has been filed with the Commission and is available for public inspection.

a. *Type of Application:* Subsequent Minor License.

b. *Project No.:* P–2955–011.

c. *Date filed:* February 28, 2020.

d. *Applicant:* City of Watervliet, New York.

e. *Name of Project:* Normanskill Hydropower Project.

f. *Location:* The project is located on the Normans Kill in Guilderland, Albany County, New York. The project does not occupy any federal land.

g. *Filed Pursuant to:* Federal Power Act 16 U.S.C. 791(a)–825(r).

h. *Applicant Contact:* Michele E. Stottler, Gomez and Sullivan Engineers, DPC, 399 Albany Shaker Road, Suite 203, Loudonville, NY 12211; (518) 407–0050; email—*mstottler@gomezandsullivan.com* or Joseph LaCivita, General Manager, The City of Watervliet, 2 Fifteenth Street, Watervliet, NY 12189; (518) 270–3800; email—*jlacivita@watervliet.com*.

i. *FERC Contact:* Woohee Choi at (202) 502–6336; or email at *woohee.choi@ferc.gov*.

j. *Deadline for filing scoping comments:* October 8, 2020.

The Commission strongly encourages electronic filing. Please file scoping comments using the Commission's eFiling system at *http://www.ferc.gov/docs-filing/efiling.asp.* Commenters can submit brief comments up to 6,000 characters, without prior registration, using the eComment system at *http://www.ferc.gov/docs-filing/ecomment.asp.* You must include your name and contact information at the end of your comments. For assistance, please contact FERC Online Support at *FERCOnlineSupport@ferc.gov,* (866) 208–3676 (toll free), or (202) 502–8659 (TTY). In lieu of electronic filing, you may submit a paper copy. Submissions sent via the U.S. Postal Service must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 888 First Street NE, Room 1A, Washington, DC 20426. Submissions sent via any other carrier must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 12225 Wilkins Avenue, Rockville, Maryland 20852. The first page of any filing should include docket number P–2955–011.

The Commission's Rules of Practice require all intervenors filing documents with the Commission to serve a copy of that document on each person on the official service list for the project. Further, if an intervenor files comments or documents with the Commission relating to the merits of an issue that may affect the responsibilities of a particular resource agency, they must also serve a copy of the document on that resource agency.

k. This application is not ready for environmental analysis at this time.

l. The Normanskill Project consists of the following existing facilities: (1) A 380-foot-long reinforced concrete Ambursen-type dam with a 306-foot-long overflow section having a crest elevation of 259 feet National Geodetic Vertical Datum of 1929 (NGVD29) surmounted by 3-foot-high flashboards; (2) a 380-acre reservoir with a gross volume of 3,600 acre-feet at the normal maximum pool elevation of 262 feet NGVD29; (3) an intake structure and sluiceway; (4) a 700-foot-long, 6-foot-diameter, concrete-encased steel, buried penstock; (5) a reinforced concrete underground powerhouse containing a single 1,250-kilowatt tube-type generating unit; (6) a 600-foot-long, 2.4-kilovolt (kV) transmission line; (7) a 2.4/13.2-kV transformer bank; and (8) appurtenant facilities.

m. In addition to publishing the full text of this notice in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents of this notice, as well as other documents in the proceeding (*e.g.,* scoping document) via the internet through the Commission's Home Page (*http://www.ferc.gov*) using the ''eLibrary'' link. Enter the docket number excluding the last three digits in the docket number field to access the document (P–2955). At this time, the Commission has suspended access to the Commission's Public Reference Room due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID–19) issued by the President on March 13, 2020. For assistance, contact FERC at *FERCOnlineSupport@ferc.gov* or call toll-free, (886) 208–3673 or (202) 502–8659 (TTY).

n. You may also register online at *http://www.ferc.gov/docs-filing/esubscription.asp* to be notified via email of new filings and issuances related to this or other pending projects. For assistance, contact FERC Online Support.

o. Scoping Process

The Commission staff intends to prepare a single Environmental Assessment (EA) for the Normanskill Hydroelectric Project in accordance with the National Environmental Policy Act. The EA will consider both site-specific and cumulative environmental impacts and reasonable alternatives to the proposed action.

Commission staff does not propose to conduct any on-site scoping meetings at this time. Instead, we are soliciting comments, recommendations, and information, on the Scoping Document (SD) issued on September 8, 2020.

Copies of the SD outlining the subject areas to be addressed in the EA were distributed to the parties on the Commission's mailing list and the applicant's distribution list. Copies of the SD may be viewed on the web at *http://www.ferc.gov* using the ''eLibrary'' link. Enter the docket number excluding the last three digits in the docket number field to access the document. For assistance, call 1–866–208–3676 or for TTY, (202) 502–8659.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20164 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Docket No. ER20–2830–000]

PPM Roaring Brook, LLC; Supplemental Notice That Initial Market-Based Rate Filing Includes Request For Blanket Section 204 Authorization

This is a supplemental notice in the above-referenced PPM Roaring Brook, LLC's application for market-based rate authority, with an accompanying rate tariff, noting that such application includes a request for blanket authorization, under 18 CFR part 34, of future issuances of securities and assumptions of liability.

Any person desiring to intervene or to protest should file with the Federal Energy Regulatory Commission, 888 First Street NE, Washington, DC 20426, in accordance with Rules 211 and 214 of the Commission's Rules of Practice and Procedure (18 CFR 385.211 and 385.214). Anyone filing a motion to intervene or protest must serve a copy of that document on the Applicant.

Notice is hereby given that the deadline for filing protests with regard to the applicant's request for blanket authorization, under 18 CFR part 34, of future issuances of securities and assumptions of liability, is September 28, 2020.

The Commission encourages electronic submission of protests and interventions in lieu of paper, using the FERC Online links at *http://www.ferc.gov.* To facilitate electronic service, persons with internet access who will eFile a document and/or be listed as a contact for an intervenor must create and validate an eRegistration account using the eRegistration link. Select the eFiling link to log on and submit the intervention or protests.

Persons unable to file electronically may mail similar pleadings to the Federal Energy Regulatory Commission, 888 First Street NE, Washington, DC 20426. Hand delivered submissions in docketed proceedings should be delivered to Health and Human Services, 12225 Wilkins Avenue, Rockville, Maryland 20852.

In addition to publishing the full text of this document in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents of this document via the internet through the Commission's Home Page (*http://ferc.gov*) using the ''eLibrary'' link. Enter the docket number excluding the last three digits in the docket number field to access the document. At this time, the Commission has suspended access to the Commission's Public Reference Room, due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID–19), issued by the President on March 13, 2020. For assistance, contact the Federal Energy Regulatory Commission at *FERCOnlineSupport@ferc.gov* or call toll-free, (886) 208–3676 or TYY, (202) 502–8659.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20167 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Docket No. CP20–518–000]

PennEast Pipeline Company, LLC; Notice of Petition for Declaratory Order

Take notice that on August 31, 2020, pursuant to Rule 207(a)(2) of the Federal Energy Regulatory Commission's (Commission) Rules of Practice and Procedure, Robert Kaiser (Petitioner) hereby submits a petition for declaratory order (Petition) requesting the Commission issue a declaratory order putting a hold on PennEast Pipeline Company, LLC's (PennEast) eminent domain authority until PennEast has received the necessary permits and authorizations to commence construction and requesting an exemption from the filing fee, as more fully explained in the petition.

Any person desiring to intervene or to protest this filing must file in accordance with Rules 211 and 214 of the Commission's Rules of Practice and Procedure (18 CFR 385.211, 385.214). Protests will be considered by the Commission in determining the appropriate action to be taken, but will not serve to make protestants parties to the proceeding. Any person wishing to become a party must file a notice of intervention or motion to intervene, as appropriate. Such notices, motions, or protests must be filed on or before the comment date. Anyone filing a motion to intervene or protest must serve a copy of that document on the Petitioner.

The Commission encourages electronic submission of protests and interventions in lieu of paper using the ''eFiling'' link at *http://www.ferc.gov.* Persons unable to file electronically may mail similar pleadings to the Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426. Hand delivered submissions in docketed proceedings should be delivered to Health and Human Services, 12225 Wilkins Avenue, Rockville, Maryland 20852.

In addition to publishing the full text of this document in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents of this document via the internet through the Commission's Home Page (*http://ferc.gov*) using the ''eLibrary'' link. Enter the docket number excluding the last three digits in the docket number field to access the document. At this time, the Commission has suspended access to the Commission's Public Reference Room, due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID–19), issued by the President on March 13, 2020. For assistance, contact the Federal Energy Regulatory Commission at *FERCOnlineSupport@ferc.gov* or call toll-free, (886) 208–3676 or TYY, (202) 502–8659.

Comment Date: 5:00 p.m. Eastern time on September 30, 2020.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20168 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Docket No. IC20–25–000]

Commission Information Collection Activities (Ferc–717); Comment Request; Extension

AGENCY: Federal Energy Regulatory Commission, Energy.

ACTION: Notice of extension information collection and request for comments.

SUMMARY: In compliance with the requirements of the Paperwork Reduction Act of 1995, the Federal Energy Regulatory Commission (''Commission'' or ''FERC'') is soliciting public comment on the extension to the information collection, FERC–717 (Standards for Business Practices and Communication Protocols for Public Utilities) which will be submitted to the Office of Management and Budget (OMB) for a review of the information collection requirements.

DATES: Comments on the collection of information are due November 13, 2020.

ADDRESSES: Please submit a copy of your comments to the Commission (identified by Docket No. IC20–25–000) by one of the following methods:

• *eFiling at Commission's website: http://www.ferc.gov/docs-filing/efiling.asp.*

• *U.S. Postal Service Mail:* Persons unable to file electronically may mail similar pleadings to the Federal Energy Regulatory Commission, 888 First Street NE, Washington, DC 20426.

• Effective 7/1/2020, delivery of filings other than by eFiling or the U.S.

Postal Service should be delivered to Health and Human Services, 12225 Wilkins Avenue, Rockville, Maryland 20852.

Instructions: All submissions must be formatted and filed in accordance with submission guidelines at: *http://www.ferc.gov.* For user assistance contact FERC Online Support by email at *ferconlinesupport@ferc.gov,* or by phone at: (866) 208–3676 (toll-free), or (202) 502–8659 for TTY.

Docket: Users interested in receiving automatic notification of activity in this docket or in viewing/downloading comments and issuances in this docket may do so at *http://www.ferc.gov/docs-filing/docs-filing.asp.*

FOR FURTHER INFORMATION: Ellen Brown may be reached by email at *DataClearance@FERC.gov,* telephone at (202) 502–8663.

SUPPLEMENTARY INFORMATION:

Title: FERC–717, Standards for Business Practices and Communication Protocols for Public Utilities.

OMB Control No.: 1902–0173.

Type of Request: Three-year approval of the FERC–717 information collection requirements with no changes to the current reporting requirements.[1]

Abstract: The Commission directs all public utilities that own, control or operate facilities for transmitting energy in interstate commerce to provide certain types of information regarding their transmission operations on an Open Access Same-time Information System (OASIS). The Commission does not believe that open-access nondiscriminatory transmission services can be completely realized until it removes real-world obstacles that prevent transmission customers from competing effectively with the Transmission Provider. One of the obstacles is unequal access to transmission information. The Commission believes that transmission customers must have simultaneous access to the same information available to the Transmission Provider if truly nondiscriminatory transmission services are to be a reality.

The Commission also established Standards of Conduct requiring that personnel engaged in transmission system operations function independently from personnel engaged in marketing functions. The Standards of Conduct were designed to prevent employees of a public utility (or any of its affiliates) engaged in marketing functions from preferential access to OASIS-related information or from engaging in unduly discriminatory business practices. Companies were required to separate their transmission operations/reliability functions from their marketing/merchant functions and prevent system operators from providing merchant employees and employees of affiliates with transmission-related information not available to all customers at the same time through public posting on the OASIS.

Type of Respondents: Transmission Owners and Transmission Operators.

Estimate of Annual Burden[2]: The Commission estimates an adjustment in the annual public reporting burden for the FERC–717. The adjustment is due to Transmission Providers being allowed to file responses jointly or individually. The Transmission Provider may delegate this responsibility to a Responsible Party such as another Transmission Provider, an Independent System Operator, a Regional Transmission Group, or a Regional Reliability Council. The number comprise two separate entities: Transmission Owners and Transmission Operators. The responses submitted are our best estimate of the Transmission Operators and remaining individual Transmission Owners. The rationale is that some Transmission Owners have elected to turn over operational control of their collective transmission systems to Transmission Operators, including RTOs/ISOs (as authorized in 18 CFR 37.5). These Transmission Operators offer OASIS access to the collective systems facilitating a single OASIS transmission request serving multiple transmission systems. As a result of these efficiency gains, the lower respondent count is appropriate.

As a result of the efficiency gains, and an overestimate of the respondents in our past requests, we are submitting a more accurate number of respondents. The estimate below reflects the work associated with the current information collection requirements:

FERC–717, STANDARDS FOR BUSINESS PRACTICES AND COMMUNICATION PROTOCOLS FOR PUBLIC UTILITIES[3]

Information collection requirements	Number of respondents (1)	Annual number of responses per respondent (2)	Total number of responses (1) * (2) = (3)	Average burden hours & cost per response[4] (4)	Total annual burden hours & total annual cost (3) * (4) = (5)
FERC–717	162	1	162	30 hrs.; $2,490	4,860 hrs.; $403,380.
FERC–717 (compliance with standards, one-time)[5]	165	1	165	10 hrs.;[6] $830	1,650 hrs.; $136,950.
Total			327		6,510 hrs.; $540,330.

Comments: Comments are invited on: (1) Whether the collection of information is necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (2) the accuracy of the agency's estimate of the burden and cost of 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 collection; and (4) ways to minimize the burden of the collection of information on those who are to respond, including the use

[1] This collection notice does not address the NOPR for RM05–29 and RM05–30.

[2] Burden is defined as the total time, effort, or financial resources expended by persons to generate, maintain, retain, or disclose or provide information to or for a Federal agency. For further explanation of what is included in the information collection burden, refer to 5 Code of Federal Regulations 1320.3.

[3] This collection includes the one-time burden (over a 3 year period of time) for the Final Rule RM05–25,05–26,05–27 [ICR Reference No: 202002–1902–006]

[4] The Commission staff thinks that the average respondent for this collection is similarly situated to the Commission, in terms of salary plus benefits. Based upon FERC's FY 2020 annual average of $172,329, (for salary plus benefits), the average hourly cost is $83/hour.

[5] FERC–717 corresponds to OMB Control No. 1902–0173 that identifies the information collection associated with Standards for Business Practices and Communication Protocols for Public Utilities.

[6] The 30-hour estimate was developed in Docket No. RM05–5–013, when the Commission prepared its estimate of the scope of work involved in transitioning to the NAESB Version 002.1 Business Practice Standards. See Order No. 676–E, 129 FERC 61,162 at P 134. (FERC–717, 165 * 30 = 4,950 hrs./3 = 1,650 hrs./year)

of automated collection techniques or other forms of information technology.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20166 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Docket No. IC20–10–000]

Commission Information Collections Activities (Ferc Form Nos. 2 And 2–A); Comment Request; Extension; Errata Notice

AGENCY: Federal Energy Regulatory Commission.

ACTION: Errata notice for information collections and request for comments.

SUMMARY: In compliance with the requirements of the Paperwork Reduction Act of 1995, the Federal Energy Regulatory Commission (Commission or FERC) is soliciting public comment on currently approved information collections, FERC Form No. 2 (Annual Report for Major Natural Gas Companies) and FERC Form No. 2–A (Annual Report for Non-Major Natural Gas Companies). This notice corrects and replaces the 30-day notice published on July 20, 2020. The 60-day notice was published on April 30, 2020 and the initial 30-day notice published on July 20, 2020. The intial 30-day notice erroneously omitted the burden associated with a Final rule approved September 9, 2019. In order to correct the previously published notices, FERC is providing the opportunity for an additional 30-day comment period.

DATES: Comments on the collections of information are due October 14, 2020.

ADDRESSES: You may submit written comments on FERC Form Nos. 2 and 2–A to the Office of Management and Budget (OMB) through *www.reginfo.gov/public/do/PRAMain,* Attention: Federal Energy Regulatory Commission Desk Officer. Please identify the OMB control numbers (1902–0028 and 1902–0030) in the subject line. Your comments should be sent within 30 days of publication of this notice in the **Federal Register**.

Please submit copies of your comments to the Commission (identified by Docket No. IC20–10–000) by one of the following methods:

- *eFiling at Commission's Website: http://www.ferc.gov*.
- *U.S. Postal Service Mail:* Persons unable to file electronically may mail similar pleadings to the Federal Energy Regulatory Commission, 888 First Street NE, Washington, DC 20426.
- Effective 7/1/2020, delivery of filings other than by eFiling or the U.S. Postal Service should be delivered to Health and Human Services, 12225 Wilkins Avenue, Rockville, Maryland 20852.

Instructions: All submissions must be formatted and filed in accordance with submission guidelines at: *https://www.ferc.gov/filing-instructions.* For user assistance, contact FERC Online Support by email at *ferconlinesupport@ferc.gov,* or by phone at: (866) 208–3676 (toll-free).

Docket: Users interested in receiving automatic notification of activity in this docket or in viewing/downloading comments and issuances in this docket may do so at *http://www.ferc.gov/docs-filing/docs-filing.asp.*

FOR FURTHER INFORMATION CONTACT: Ellen Brown may be reached by email at *DataClearance@FERC.gov* and telephone at (202) 502–8663.

SUPPLEMENTARY INFORMATION:

Title: FERC Form No. 2, Annual Report for Major Natural Gas Companies, and FERC Form No. 2–A, Annual Report for Non-Major Natural Gas Companies.

OMB Control Nos.: 1902–0028 (FERC Form No. 2), and 1902–0030 (FERC Form No. 2–A)

Type of Request: Three-year extension of the FERC Form No. 2 and FERC Form No. 2–A information collections requirements without a change to the current reporting and recordkeeping requirements.

Abstract: Pursuant to sections 8, 10 and 14 of the Natural Gas Act (NGA), (15 U.S.C. 717g, 717i, and 717m), the Commission is authorized to conduct investigations and collect and record data, and to prescribe rules and regulations concerning accounts, records and memoranda as necessary or appropriate for purposes of administering the NGA. The Commission may prescribe a system of accounts for jurisdictional companies and, after notice and opportunity for hearing, may determine the accounts in which particular outlays and receipts will be entered, charged or credited.

The Commission collects FERC Form Nos. 2 and 2–A information as prescribed in 18 CFR 260.1 and 18 CFR 260.2. These forms provide information concerning a company's current performance, compiled using the Commission's Uniform System of Accounts (USofA).[1] FERC Form No. 2 is filed by ''Major'' natural gas companies that have combined natural gas transported or stored for a fee that exceeds 50 million Dekatherms in each of the three previous calendar years. FERC Form No. 2–A is filed by ''Non-Major'' natural gas companies that do not meet the filing threshold for the FERC Form No. 2, but have total gas sales or volume transactions that exceeds 200,000 Dekatherms in each of the three previous calendar years.[2]

The forms provide information concerning a company's financial and operational information. The forms contain schedules which include a basic set of financial statements: Comparative Balance Sheet, Statement of Income and Retained Earnings, Statement of Cash Flows, and the Statement of Comprehensive Income and Hedging Activities. Supporting schedules containing supplementary information are filed, including revenues and the related quantities of products sold or transported; account balances for various operating and maintenance expenses; selected plant cost data; and other information.

The information collected assists the Commission in the administration of its jurisdictional responsibilities and is used by Commission staff, state regulatory agencies, customers, financial analysts and others in the review of the financial condition of regulated companies. The information is also used in various rate proceedings, industry analyses and in the Commission's audit programs and as appropriate, for the computation of annual charges. The information is made available to the public, interveners and all interested parties to assist in the proceedings before the Commission. For financial information to be useful to the Commission, it must be understandable, relevant, reliable and timely. The Form Nos. 2 and 2–A financial statements are prepared in accordance with the Commission's USofA and related regulations, and provide data that enables the Commission to develop and monitor cost-based rates, analyze costs of different services and classes of assets, and compare costs across lines of business. The use of the USofA permits natural gas companies to account for

[1] *See* 18 CFR part 201 (Uniform System of Accounts Prescribed for Natural Gas Companies Subject to the Provisions of the Natural Gas Act).

[2] FERC Form Nos. 2 and 2–A are part of the ''Forms Refresh'' effort, which is a separate activity and not addressed here. See Revisions to the Filing Process for Commission Forms, 166 FERC ¶ 61,027 (2019) (started in Docket No. AD15–11–000 and ongoing in Docket No. RM19–12–000). OMB issued its decisions on the Forms Refresh Final Rule in Docket No. RM19–12–000 on June 27, 2019.

similar transactions and events in a consistent manner, and to communicate those results to the Commission on a periodic basis. Comparability of data and financial statement analysis for a particular entity from one period to the next, or between entities, within the same industry, would be difficult to achieve if each company maintained its own accounting records using dissimilar accounting methods and classifications to record similar transactions and events. In summary, without the information collected in the forms, it would be difficult for the Commission to ensure, as required by the NGA, that a pipeline's rates remain just and reasonable, respond to Congressional and outside inquires, and make decisions in a timely manner. On April 30, 2020, the Commission published a Notice in the **Federal Register** in Docket No. IC20–10–000 requesting public comments.[3] The Commission received no public comments.

Note: This notice replaces and corrects the 30-day notice published on July 20, 2020 (85FR43831); no public comments were received. The burden and cost estimates have been corrected to include the industry burden of preparing and submitting in XBRL carried over from RM19–12 (approved by OMB 9/2019). The changes are reflected within the table below.

Type of Respondent: Major and Non-Major Natural Gas Companies.

Estimate of Annual Burden:[4] The Commission estimates the annual public reporting burden and cost[5] for the information collections as shown in the following table:

Information collections (FERC Form No.)	Number of respondents (1)	Annual number of responses per respondent (2)	Total number of responses (1) * (2) = (3)	Average burden & cost ($) per response (4)	Total annual burden hours & cost ($)[6] (3) * (4) = (5)	Annual cost per respondent ($) (5) ÷ (1)
Form No. 2—representing 100 respondents						
Burden to Comply with Filing Requirement	100	1	100	1,671.67 hrs.; $133,734	167,167 hrs.; $13,373,360	133,734
Burden to Prepare and Submit in XBRL (represented using the same number of respondents and responses normally received annually).	100	1	100	42.66 hrs.; $3,413	4,266 hrs.; $341,280	3,413
Form No. 2 Total	100	1	100	1,714.32 hrs.; $137,147	171,433 hrs.; $13,714,700	137,147
Form No. 2–A—representing 81 respondents						
Burden to Comply with Filing Requirement	81	1	81	296 hrs.; $23,680	23,976 hrs.; $1,918,080	23,680
Burden to Prepare and Submit in XBRL (represented using the same number of respondents and responses normally received annually).	81	1	81	42.66 hrs.; $3,413	3,455.46 hrs.; $276,453	3,413
Form No. 2–A Total	81	1	81	338.66 hrs.; $27,093	27,431.46 hrs.; $2,194, 533	27,093

- The number of annual responses related to the FERC Form Nos. 2 and 2–A is 181 responses.
- The industry burden of complying with the filing requirement is 167,167 hours (rounded) for FERC Form No. 2 and 23,976 hours for FERC Form No. 2–A.
- The industry burden of preparing and submitting in XBRL carried over from RM19–12 (approved by OMB 9/2019) 100 hours per form for the first year plus 14 hours per form for the remaining 2 years. The annual estimated total XBRL hours (100 + 14 + 14 = 128; 128 hrs./3 yrs. = 42.66 hrs. per respondent per response) is 4,266 hours for FERC Form No. 2 and 3,455.46 hours for FERC Form No. 2–A.

Comments: Comments are invited on: (1) Whether the collections of information are necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (2) the accuracy of the agency's estimate of the burden and cost of the collections of information, including the validity of the methodology and assumptions used; (3) ways to enhance the quality, utility and clarity of the information collections; and (4) ways to minimize the burden of the collections of information on those who are to respond, including the use of automated collection techniques or other forms of information technology.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20170 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Docket No. CP20–27–000]

North Baja Pipeline, LLC; Notice of Availability of the Environmental Assessment for the Proposed North Baja Xpress Project

The staff of the Federal Energy Regulatory Commission (FERC or Commission) has prepared an environmental assessment (EA) for the North Baja XPress Project, proposed by North Baja Pipeline, LLC (North Baja) in the above-referenced docket. North Baja requests authorization to modify an existing compressor station in La Paz County, Arizona, as well as install additional flow measurement facilities and piping modifications at two existing meter stations in La Paz County, Arizona, and Imperial County, California, respectively. The project would enable the transport of 495,000 dekatherms per day to the United States/Mexico border. North Baja states that the purpose of the project is to create capacity to meet growing market demand and provide transportation of feed gas for the Energia Costa Azul liquefied natural gas terminal in Baja California, Mexico.

The EA assesses the potential environmental effects of the construction and operation of the North Baja XPress Project in accordance with the requirements of the National Environmental Policy Act (NEPA). The FERC staff concludes that approval of the proposed project, with appropriate

[3] 85 FR 23954.

[4] Burden is defined as the total time, effort, or financial resources expended by persons to generate, maintain, retain, or disclose or provide information to or for a Federal agency. For further explanation of what is included in the information collections burden, refer to 5 Code of Federal Regulations 1320.3.

[5] The Commission staff believes the FERC FTE (full-time equivalent) average cost for wages plus benefits is representative of the corresponding cost for the industry respondents. Based upon the FERC's 2019 average cost for salary plus benefits, the average hourly cost is $80/hour.

[6] Every cost figure in this column is rounded to the nearest dollar.

mitigating measures, would not constitute a major federal action significantly affecting the quality of the human environment.

The U.S. Department of the Interior Bureau of Land Management (BLM) participated as a cooperating agency in the preparation of the EA. Cooperating agencies have jurisdiction by law or special expertise with respect to resources potentially affected by the proposal and participate in the NEPA analysis. The BLM will adopt and use the EA to consider the issuance of a right-of-way grant for the use of a potential temporary workspace on BLM-administered public lands adjacent to the Ogilby Meter Station. North Baja submitted an application requesting a right-of-way for use of a temporary workspace on BLM-administered public lands.

The proposed North Baja XPress Project includes the following facilities:

- The construction of one new 31,900-horsepower compressor unit and restaging of two existing 7,700-horsepower compressor units at North Baja's existing Ehrenberg Compressor Station in La Paz County, Arizona; and
- the addition of flow measurement facilities and piping modifications at North Baja's existing El Paso and Ogilby Meter Stations in La Paz County, Arizona and Imperial County, California, respectively.

The Commission mailed a copy of the *Notice of Availability* for the project to federal, state, and local government representatives and agencies; elected officials; environmental and public interest groups; Native American tribes; potentially affected landowners and other interested individuals and groups; and newspapers and libraries in the project area. The EA is only available in electronic format. It may be viewed and downloaded from the FERC's website (*www.ferc.gov*), on the natural gas environmental documents page (*https://www.ferc.gov/industries-data/naturalgas/environment/environmental-documents*). In addition, the EA may be accessed by using the eLibrary link on the FERC's website. Click on the eLibrary link (*https://www.ferc.gov/ferc-online/elibrary/overview*), select ''General Search'' and enter the docket number in the ''Docket Number'' field, excluding the last three digits (*i.e.* CP20–27). Be sure you have selected an appropriate date range. For assistance, please contact FERC Online Support at *FercOnlineSupport@ferc.gov* or toll free at (866) 208–3676, or for TTY, contact (202) 502–8659.

The EA is not a decision document. It presents Commission staff's independent analysis of the environmental issues for the Commission to consider when addressing the merits of issues raised in this proceeding. Any person wishing to comment on the EA may do so. Your comments should focus on the EA's disclosure and discussion of potential environmental effects, reasonable alternatives, and measures to avoid or lessen environmental impacts. The more specific your comments, the more useful they will be. To ensure that the Commission has the opportunity to consider your comments prior to making its decision on this project, it is important that we receive your comments in Washington, DC on or before 5:00 p.m. Eastern Time on October 8, 2020.

For your convenience, there are three methods you can use to file your comments to the Commission. The Commission encourages electronic filing of comments and has staff available to assist you at (866) 208–3676 or *FercOnlineSupport@ferc.gov.* Please carefully follow these instructions so that your comments are properly recorded.

(1) You can file your comments electronically using the eComment feature on the Commission's website (*www.ferc.gov*) under the link to FERC Online. This is an easy method for submitting brief, text-only comments on a project;

(2) You can also file your comments electronically using the eFiling feature on the Commission's website (*www.ferc.gov*) under the link to FERC Online. With eFiling, you can provide comments in a variety of formats by attaching them as a file with your submission. New eFiling users must first create an account by clicking on ''eRegister.'' You must select the type of filing you are making. If you are filing a comment on a particular project, please select ''Comment on a Filing''; or

(3) You can file a paper copy of your comments by mailing them to the Commission. Be sure to reference the project docket number (CP20–27–000) on your letter. Submissions sent via the U.S. Postal Service must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 888 First Street NE, Room 1A, Washington, DC 20426. Submissions sent via any other carrier must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 12225 Wilkins Avenue, Rockville, MD 20852.

Filing environmental comments will not give you intervenor status, but you do not need intervenor status to have your comments considered. Only intervenors have the right to seek rehearing or judicial review of the Commission's decision. At this point in this proceeding, the timeframe for filing timely intervention requests has expired. Any person seeking to become a party to the proceeding must file a motion to intervene out-of-time pursuant to Rule 214(b)(3) and (d) of the Commission's Rules of Practice and Procedures (18 CFR 385.214(b)(3) and (d)) and show good cause why the time limitation should be waived. Motions to intervene are more fully described at *https://www.ferc.gov/ferc-online/ferc-online/how-guides.*

Additional information about the project is available from the Commission's Office of External Affairs, at (866) 208–FERC, or on the FERC website (*www.ferc.gov*) using the eLibrary link. The eLibrary link also provides access to the texts of all formal documents issued by the Commission, such as orders, notices, and rulemakings.

In addition, the Commission offers a free service called eSubscription which allows you to keep track of all formal issuances and submittals in specific dockets. This can reduce the amount of time you spend researching proceedings by automatically providing you with notification of these filings, document summaries, and direct links to the documents. Go to *https://www.ferc.gov/ferc-online/overview* to register for eSubscription.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20169 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Project No. 14514–003]

Community of Elfin Cove Non Profit Corporation, DBA Elfin Cove Utility Commission; Notice of Application Tendered for Filing With the Commission and Soliciting Additional Study Requests

Take notice that the following hydroelectric application has been filed with the Commission and is available for public inspection.

a. *Type of Application:* Original minor license.

b. *Project No.:* P–14514–003.

c. *Date filed:* August 24, 2020.

d. *Applicant:* Community of Elfin Cove Non Profit Corporation, DBA Elfin Cove Utility Commission.

e. *Name of Project:* Crooked Creek and Jim's Lake Hydroelectric Project.

f. *Location:* On Crooked Creek and Jim's Lake, near the community of Elfin Cove, in the Sitka Recording District, Unorganized Borough, Alaska. The project would occupy 13.98 acres of federal land in the Tongass National Forest, managed by the U.S. Department of Agriculture's Forest Service.

g. *Filed Pursuant to:* Federal Power Act 16 U.S.C. 791(a)–825(r).

h. *Applicant Contact:* Mr. Joel Groves, Polarconsult Alaska, Inc., 1503 W 33rd Avenue, #310, Anchorage, Alaska 99503; phone: (907) 258–2420 ext. 204.

i. *FERC Contact:* John Matkowski at (202) 502–8576; or email at *john.matkowski@ferc.gov.*

j. *Cooperating agencies:* Federal, state, local, and tribal agencies with jurisdiction and/or special expertise with respect to environmental issues that wish to cooperate in the preparation of the environmental document should follow the instructions for filing such requests described in item l below. Cooperating agencies should note the Commission's policy that agencies that cooperate in the preparation of the environmental document cannot also intervene. *See,* 94 FERC ¶ 61,076 (2001).

k. Pursuant to section 4.32(b)(7) of 18 CFR of the Commission's regulations, if any resource agency, Indian Tribe, or person believes that an additional scientific study should be conducted in order to form an adequate factual basis for a complete analysis of the application on its merit, the resource agency, Indian Tribe, or person must file a request for a study with the Commission not later than 60 days from the date of filing of the application, and serve a copy of the request on the applicant.

l. Deadline for filing additional study requests and requests for cooperating agency status: October 23, 2020.

The Commission strongly encourages electronic filing. Please file additional study requests and requests for cooperating agency status using the Commission's eFiling system at *http://www.ferc.gov/docs-filing/efiling.asp.* For assistance, please contact FERC Online Support at *FERCOnlineSupport@ferc.gov,* (866) 208–3676 (toll free), or (202) 502–8659 (TTY).

m. The application is not ready for environmental analysis at this time.

n. The proposed project would consist of two developments, the Upper System and the Lower System.

The Upper System development would consist of the following new facilities: (1) A 16-foot-long, 6-foot-diameter intake structure to divert up to five cubic feet per second (cfs) from Crooked Creek; (2) a 1,050-foot-long, 14-inch-diameter buried penstock extending between the intake structure and the powerhouse; (3) a 16-foot-long, 20-foot-wide, 20-foot-high powerhouse containing a 35-kilowatt (kW) crossflow turbine; (4) a tailrace discharging flows into Jim's Lake; and (5) appurtenant facilities.

The Lower System development would consist of the following facilities: (1) 225-foot-long, 18-foot-high rock-fill dam and intake structure at the outlet of Jim's Lake to divert up to 6.5 cfs from Jim's Lake; (2) a 2,550-foot-long, 16 to 18-inch-diameter buried penstock extending between the intake and the powerhouse; (3) 20-foot-long, 28-foot-wide, 14-foot-high powerhouse containing a 105-kW impulse turbine; (4) a tailrace discharging flows into Port Althorp; and (5) appurtenant facilities.

The project would also include an underground 8,800-foot-long, 7.2/12.47-kilovolt (kV) transmission line extending from the project powerhouses at each of the developments to Elfin Cove's existing 7.2/12.47-kV transmission line. The project would generate an average of 788.3 megawatt-hours annually.

o. In addition to publishing the full text of this document in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents via the internet through the Commission's Home Page (*http://www.ferc.gov*) using the ''eLibrary'' link. Enter the docket number excluding the last three digits in the docket number field to access the document. At this time, the Commission has suspended access to the Commission's Public Reference Room, due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID–19), issued by the President on March 13, 2020. For assistance, contact FERC at *FERCOnlineSupport@ferc.gov* or call toll-free, (866) 208–3676 or TYY, (202) 502–8659.

You may also register online at *http://www.ferc.gov/docs-filing/esubscription.asp* to be notified via email of new filings and issuances related to this or other pending projects. For assistance, contact FERC Online Support.

p. *Procedural schedule:* The application will be processed according to the following preliminary schedule. Revisions to the schedule will be made as appropriate.

Issue Deficiency Letter (if necessary)—November 2020
Request Additional Information—November 2020
Issue Acceptance Letter—February 2021
Issue Scoping Document 1 for comments—March 2021
Request Additional Information (if necessary)—May 2021
Issue Scoping Document 2—June 2021
Issue Notice of Ready for Environmental Analysis—June 2021
Commission issues Environmental Assessment—December 2021

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20172 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Project No. 7274–034]

Town of Wells; Notice of Intent To File License Application, Filing of Pre-Application Document, Approving Use of the Traditional Licensing Process

a. *Type of Filing:* Notice of Intent to File License Application and Request to Use the Traditional Licensing Process.

b. *Project No.:* 7274–034.

c. *Date Filed:* July 28, 2020.

d. *Submitted By:* Town of Wells.

e. *Name of Project:* Lake Algonquin Hydroelectric Project.

f. *Location:* On the Sacandaga River in the Town of Wells, Hamilton County, New York. The project does not occupy any federal land.

g. *Filed Pursuant to:* 18 CFR 5.3 of the Commission's regulations.

h. *Potential Applicant Contact:* Nicholas Mauro, Town of Wells, 1438 State Route 30, Wells, NY 12190; (518) 775–9390; email—*nick-mauro@townofwells.org.*

i. *FERC Contact:* Samantha Pollak at (202) 502–6419; or email at *samantha.pollak@ferc.gov.*

j. The Town of Wells filed its request to use the Traditional Licensing Process on July 28, 2020. The Town of Wells provided public notice of its request on July 20, 2020. In a letter dated September 8, 2020, the Director of the Division of Hydropower Licensing approved the Town of Wells' request to use the Traditional Licensing Process.

k. With this notice, we are initiating informal consultation with the U.S. Fish and Wildlife Service under section 7 of the Endangered Species Act and the joint agency regulations thereunder at 50 CFR, Part 402. We are also initiating consultation with the New York State Historic Preservation Officer, as required by section 106, National Historic Preservation Act, and the implementing regulations of the Advisory Council on Historic Preservation at 36 CFR 800.2.

l. With this notice, we are designating the Town of Wells as the Commission's non-federal representative for carrying out informal consultation pursuant to section 7 of the Endangered Species Act and consultation pursuant to section 106 of the National Historic Preservation Act.

m. The Town of Wells filed a Pre-Application Document (PAD; including a proposed process plan and schedule) with the Commission, pursuant to 18 CFR 5.6 of the Commission's regulations.

n. A copy of the PAD may be viewed on the Commission's website (*http://www.ferc.gov*), using the ''eLibrary'' link. Enter the docket number, excluding the last three digits in the docket number field, to access the document. At this time, the Commission has suspended access to the Commission's Public Reference Room, due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID–19), issued by the President on March 13, 2020. For assistance, contact FERC Online Support at *FERCOnlineSupport@ferc.gov,* (866) 208 3676 (toll free), or (202) 502–8659 (TTY).

o. The licensee states its unequivocal intent to submit an application for a subsequent license for Project No. 7274. Pursuant to 18 CFR 16.20, each application for a subsequent license and any competing license applications must be filed with the Commission at least 24 months prior to the expiration of the existing license. All applications for license for this project must be filed by July 31, 2023.

p. Register online at *http://www.ferc.gov/docs-filing/esubscription.asp* to be notified via email of new filing and issuances related to this or other pending projects. For assistance, contact FERC Online Support.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20173 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

[Project No. 14635–001]

Village of Gouverneur, New York; Notice Soliciting Scoping Comments

Take notice that the following hydroelectric application has been filed with the Commission and is available for public inspection.

a. *Type of Application:* Original Minor License.

b. *Project No.:* P–14635–001.

c. *Date filed:* September 20, 2019.

d. *Applicant:* Village of Gouverneur, New York.

e. *Name of Project:* Gouverneur Hydroelectric Project (Gouverneur Project).

f. *Location:* The existing unlicensed project is located on the Oswegatchie River in the Village of Gouverneur in St. Lawrence County, New York.

g. *Filed Pursuant to:* Federal Power Act 16 U.S.C. 791(a)–825(r).

h. *Applicant Contact:* Ronald P. McDougall, Mayor, Village of Gouverneur, 33 Clinton Street, Gouverneur, NY 13642; (315) 287–1720; *ronaldpmcdougall@gmail.com.*

i. *FERC Contact:* Jody Callihan at *jody.callihan@ferc.gov* or (202) 502–8278.

j. *Deadline for filing scoping comments:* October 9, 2020.

The Commission strongly encourages electronic filing. Please file scoping comments using the Commission's eFiling system at *https://ferconline.ferc.gov/FERCOnline.aspx.* Commenters can submit brief comments up to 6,000 characters, without prior registration, using the eComment system at *https://ferconline.ferc.gov/QuickComment.aspx.* You must include your name and contact information at the end of your comments. For assistance, please contact FERC Online Support at *FERCOnlineSupport@ferc.gov,* (866) 208–3676 (toll free), or (202) 502–8659 (TTY). In lieu of electronic filing, you may submit a paper copy. Submissions sent via the U.S. Postal Service must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 888 First Street NE, Room 1A, Washington, DC 20426. Submissions sent via any other carrier must be addressed to: Kimberly D. Bose, Secretary, Federal Energy Regulatory Commission, 12225 Wilkins Avenue, Rockville, Maryland 20852. The first page of any filing should include docket number P–14635–001.

The Commission's Rules of Practice require all intervenors filing documents with the Commission to serve a copy of that document on each person on the official service list for the project. Further, if an intervenor files comments or documents with the Commission relating to the merits of an issue that may affect the responsibilities of a particular resource agency, they must also serve a copy of the document on that resource agency.

k. This application is not ready for environmental analysis at this time.

l. *Project Description:* The Gouverneur Project consists of: (1) A 250-foot-long concrete gravity dam that includes two bridge piers and three separate spillways that range in crest elevation from 403.4 to 403.7 feet North American Vertical Datum of 1988 (NAVD88); (2) an impoundment with a surface area of 109 acres at the normal pool elevation of 403.8 feet NAVD88; (3) a concrete intake structure containing two trash rack bays separated by a 2-foot-wide center pier, each containing a 14-foot-wide trash rack; (4) a 20-foot by 36-foot powerhouse integral to the dam and containing two vertical axial flow propeller type turbines rated at 100 kilowatts each and two 100-kilovolt-ampere Westinghouse generators with a power factor of 0.8; (5) two generator leads from the turbine-generator units to a switchgear at the powerhouse interconnecting with the local grid; and (6) appurtenant facilities. The project generates about 1,195 megawatt-hours annually.

m. In addition to publishing the full text of this notice in the **Federal Register**, the Commission provides all interested persons an opportunity to view and/or print the contents of this notice, as well as other documents in the proceeding (*e.g.,* scoping document) via the internet through the Commission's Home Page (*http://www.ferc.gov*) using the ''eLibrary'' link. Enter the docket number excluding the last three digits in the docket number field to access the document (P–14635). At this time, the Commission has suspended access to the Commission's Public Reference Room due to the proclamation declaring a National Emergency concerning the Novel Coronavirus Disease (COVID–19) issued by the President on March 13, 2020. For assistance, contact FERC at *FERCOnlineSupport@ferc.gov* or call toll-free, (886) 208–3673 or (202) 502–8659 (TTY).

n. You may also register online at *https://ferconline.ferc.gov/FERCOnline.aspx* to be notified via email of new filings and issuances related to this or other pending projects. For assistance, contact FERC Online Support.

o. *Scoping Process*

The Commission staff intends to prepare an Environmental Assessment (EA) for the project in accordance with the National Environmental Policy Act. The EA will consider both site-specific and cumulative environmental impacts and reasonable alternatives to the proposed action.

At this time, we do not anticipate holding on-site public or agency scoping meetings. Instead, we are soliciting your comments and suggestions on the preliminary list of issues and alternatives to be addressed in the EA, as described in scoping document 1 (SD1), issued September 8, 2020.

Copies of the SD1 outlining the subject areas to be addressed in the EA were distributed to the parties on the Commission's mailing list and the applicant's distribution list. Copies of SD1 may be viewed on the web at *http://www.ferc.gov* using the ''eLibrary'' link. Enter the docket number excluding the last three digits in the docket number field to access the document. For assistance, call 1–866–208–3676 or for TTY, (202) 502–8659.

Dated: September 8, 2020.

Kimberly D. Bose,

Secretary.

[FR Doc. 2020–20171 Filed 9–11–20; 8:45 am]

BILLING CODE 6717–01–P

ENVIRONMENTAL PROTECTION AGENCY

[CERCLA–R04–2020–2506; FRL–10014–01–Region 4]

Charlotte Bay Trading Company; Notice of Settlement

AGENCY: Environmental Protection Agency (EPA).

ACTION: Notice of proposed settlement.

SUMMARY: The United States Environmental Protection Agency (EPA) proposes to enter into a Settlement Agreement for Recovery of Past Response Costs with R.T. Godley Investments III, LLC concerning the Charlotte Bay Trading Company Site located in Charlotte, North Carolina. The settlement addresses recovery of CERCLA costs for a cleanup action performed by the EPA at the Site.

DATES: The Agency will consider public comments on the settlement until October 14, 2020. The Agency will consider all comments received and may modify or withdraw its consent to the proposed settlement if comments received disclose facts or considerations which indicate that the proposed settlement is inappropriate, improper, or inadequate.

ADDRESSES: Copies of the settlement are available from the Agency by contacting Ms. Paula V. Painter, Program Analyst, using the contact information provided in this notice or through the Agency's web page *https://www.epa.gov/aboutepa/about-epa-region-4-southeast#r4-public-notices.* Comments may be submitted by referencing the Site's name or Docket # CERCLA–04–2020–2506 through email to *Painter.Paula@epa.gov.*

FOR FURTHER INFORMATION CONTACT: Paula V. Painter at 404–562–8887.

Authority: 122(h) of the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA).

Dated: August 26, 2020.

Maurice Horsey,

Chief, Enforcement Branch, Superfund & Emergency Management Division.

[FR Doc. 2020–20139 Filed 9–11–20; 8:45 am]

BILLING CODE 6560–50–P

ENVIRONMENTAL PROTECTION AGENCY

[FRL–10013–39–OAR]

Announcing Upcoming Meeting of Mobile Sources Technical Review Subcommittee

AGENCY: Environmental Protection Agency (EPA).

ACTION: Notice.

SUMMARY: Pursuant to the Federal Advisory Committee Act, EPA announces an upcoming meeting of the Mobile Sources Technical Review Subcommittee (MSTRS), which is a subcommittee under the Clean Air Act Advisory Committee (CAAAC). This is a virtual meeting and open to the public. The meeting will include discussion of current topics and presentations about activities being conducted by EPA's Office of Transportation and Air Quality. MSTRS listserv subscribers will receive notification when the agenda is available on the Subcommittee website. To subscribe to the MSTRS listserv, send an email to *MSTRS@epa.gov.*

DATES: EPA will hold a virtual public meeting on Monday, October 19, 2020 from 9:00 a.m. to 5:00 p.m. Eastern Daylight Time (EDT). Please monitor the website *https://www.epa.gov/caaac/mobile-sources-technical-review-subcommittee-mstrs-caaac* for any changes to meeting logistics. The final meeting agenda will be posted on the website.

ADDRESSES: For information on the public meeting or to register to attend, please contact *MSTRS@epa.gov.*

FOR FURTHER INFORMATION CONTACT: Any member of the public who wishes to attend the meeting or provide comments should express this intent by emailing *MSTRS@epa.gov* no later than Thursday, October 1, 2020. Further information concerning this public meeting and general information concerning the MSTRS can be found at: *https://www.epa.gov/caaac/mobile-sources-technical-review-subcommittee-mstrs-caaac.* Other MSTRS inquiries can be directed to Julia Burch, the Designated Federal Officer for MSTRS, Office of Transportation and Air Quality, at 202–564–0961 or *burch.julia@epa.gov.*

SUPPLEMENTARY INFORMATION: During the meeting, the Subcommittee may also hear progress reports from its workgroups as well as updates and announcements on Office of Transportation and Air Quality activities of general interest to attendees.

Participation in virtual public meetings. Please note that EPA is deviating from its typical approach because the President has declared a national emergency. Because of current CDC recommendations, as well as state and local orders for social distancing to limit the spread of COVID–19, EPA cannot hold in-person public meetings at this time.

The virtual public meeting will provide interested parties the opportunity to participate in this Federal Advisory Committee meeting.

EPA is asking all meeting attendees, even those who do not intend to speak, to register for the meeting by sending an email to the address listed in the **FOR FURTHER INFORMATION CONTACT** section above, by Thursday October 1, 2020. This will help EPA ensure that sufficient participation capacity will be available.

Please note that any updates made to any aspect of the meeting logistics, including potential additional sessions, will be posted online at *https://www.epa.gov/caaac/mobile-sources-technical-review-subcommittee-mstrs-caaac.* While EPA expects the meeting to go forward as set forth above, please monitor the website for any updates.

For individuals with disabilities: For information on access or services for individuals with disabilities, please email *MSTRS@epa.gov.* To request accommodate of a disability, please email *MSTRS@epa.gov,* preferably at least 10 business days prior to the meeting, to give EPA as much time as possible to process your request.

Dated: September 8, 2020.

Julia Burch,

Designated Federal Officer, Mobile Source Technical Review Subcommittee, Office of Transportation and Air Quality.

[FR Doc. 2020–20157 Filed 9–11–20; 8:45 am]

BILLING CODE 6560–50–P

ENVIRONMENTAL PROTECTION AGENCY

[FRL–10013–89–OP]

National Environmental Justice Advisory Council; Notice of Charter Renewal

AGENCY: Environmental Protection Agency (EPA).

ACTION: Notice of charter renewal.

SUMMARY: Notice is hereby given that the Environmental Protection Agency (EPA) has determined that, in accordance with the provisions of the Federal Advisory Committee Act (FACA), the National Environmental Justice Advisory Council (NEJAC) is necessary and in the public interest in connection with the performance of duties imposed on the agency by law. Accordingly, NEJAC will be renewed for an additional two-year period. The purpose of the NEJAC is to provide independent advice and recommendations to the Administrator about issues associated with integrating environmental justice concerns into EPA's outreach activities, public policies, science, regulatory, enforcement, and compliance decisions.

FOR FURTHER INFORMATION CONTACT: Inquiries may be directed to Karen L. Martin, NEJAC Designated Federal Officer, U.S. EPA, 1200 Pennsylvania Avenue NW (Mail Code 2202A), Washington, DC 20460; by telephone at 202–564–0203; via email at *nejac@epa.gov*.

Brittany Bolen,

Associate Administrator for the Office of Policy.

[FR Doc. 2020–19764 Filed 9–11–20; 8:45 am]

BILLING CODE 6560–50–P

FEDERAL COMMUNICATIONS COMMISSION

[OMB 3060–0161, 3060–0685, 3060–1070, 3060–1272; FRS 17063]

Information Collections Being Submitted for Review and Approval to Office of Management and Budget

AGENCY: Federal Communications Commission.

ACTION: Notice and request for comments.

SUMMARY: As part of its continuing effort to reduce paperwork burdens, as required by the Paperwork Reduction Act (PRA) of 1995, the Federal Communications Commission (FCC or the Commission) invites the general public and other Federal Agencies to take this opportunity to comment on the following information collection. Pursuant to the Small Business Paperwork Relief Act of 2002, the FCC seeks specific comment on how it can further reduce the information collection burden for small business concerns with fewer than 25 employees.

DATES: Written comments and recommendations for the proposed information collection should be submitted on or before October 14, 2020.

ADDRESSES: Comments should be sent to *www.reginfo.gov/public/do/PRAMain.* Find this particular information collection by selecting ''Currently under 30-day Review—Open for Public Comments'' or by using the search function. Your comment must be submitted into *www.reginfo.gov* per the above instructions for it to be considered. In addition to submitting in *www.reginfo.gov* also send a copy of your comment on the proposed information collection to Cathy Williams, FCC, via email to *PRA@fcc.gov* and to *Cathy.Williams@fcc.gov.* Include in the comments the OMB control number as shown in the **SUPPLEMENTARY INFORMATION** below.

FOR FURTHER INFORMATION CONTACT: For additional information or copies of the information collection, contact Cathy Williams at (202) 418–2918. To view a copy of this information collection request (ICR) submitted to OMB: (1) Go to the web page *http://www.reginfo.gov/public/do/PRAMain,* (2) look for the section of the web page called ''Currently Under Review,'' (3) click on the downward-pointing arrow in the ''Select Agency'' box below the ''Currently Under Review'' heading, (4) select ''Federal Communications Commission'' from the list of agencies presented in the ''Select Agency'' box, (5) click the ''Submit'' button to the right of the ''Select Agency'' box, (6) when the list of FCC ICRs currently under review appears, look for the Title of this ICR and then click on the ICR Reference Number. A copy of the FCC submission to OMB will be displayed.

SUPPLEMENTARY INFORMATION: The Commission may not conduct or sponsor a collection of information unless it displays a currently valid Office of Management and Budget (OMB) control number. No person shall be subject to any penalty for failing to comply with a collection of information subject to the PRA that does not display a valid OMB control number.

As part of its continuing effort to reduce paperwork burdens, as required by the Paperwork Reduction Act (PRA) of 1995 (44 U.S.C. 3501–3520), the FCC invited the general public and other Federal Agencies to take this opportunity to comment on the following information collection. Comments are requested concerning: (a) Whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (b) the accuracy of the Commission's burden estimates; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology. Pursuant to the Small Business Paperwork Relief Act of 2002, Public Law 107–198, see 44 U.S.C. 3506(c)(4), the FCC seeks specific comment on how it might ''further reduce the information collection burden for small business concerns with fewer than 25 employees.''

OMB Control Number: 3060–0161.

Title: Section 73.61, AM Directional Antenna Field Strength Measurements.

Form Number: N/A.

Type of Review: Extension of a currently approved collection.

Respondents: Business and other for-profit entities.

Number of Respondents and Responses: 2,268 respondents and 2,268 responses.

Estimated Time per Response: 4–50 hours.

Frequency of Response: Recordkeeping requirement.

Total Annual Burden: 36,020 hours.

Total Annual Cost: None.

Obligation to Respond: Required to obtain or retain benefits. The statutory authority for this collection of information is contained in Sections

154(i) and 303 of the Communications Act of 1934, as amended.

Nature and Extent of Confidentiality: There is no need for confidentiality with this collection of information.

Privacy Impact Assessment: No impact(s).

Needs and Uses: The information collection requirements contained in 47 CFR 73.61 require that each AM station using directional antennas to make field strength measurement as often as necessary to ensure proper directional antenna system operation. Stations not having approved sampling systems make field strength measurements every three months. Stations with approved sampling systems must take field strength measurements as often as necessary. Also, all AM stations using directional signals must take partial proofs of performance as often as necessary. The FCC staff used the data in field inspections/investigations. AM licensees with directional antennas use the data to ensure that adequate interference protection is maintained between stations and to ensure proper operation of antennas.

OMB Control Number: 3060–0685.

Title: Updating Maximum Permitted Rates for Regulated Services and Equipment, FCC Form 1210; Annual Updating of Maximum Permitted Rates for Regulated Cable Services, FCC Form 1240.

Form Number: FCC Form 1210 and FCC Form 1240.

Type of Review: Extension of a currently approved collection.

Respondents: Business or other for-profit entities; State, Local or Tribal Government.

Number of Respondents and Responses: 3,400 respondents; 5,350 responses.

Estimated Time per Response: 1 hour to 15 hours.

Frequency of Response: Annual reporting requirement; Quarterly reporting requirement; Third party disclosure requirement.

Obligation to Respond: Required to obtain or retain benefits. The statutory authority for this collection is contained in 4(i) and 623 of Communications Act of 1934, as amended.

Total Annual Burden: 44,800 hours.

Total Annual Cost: $3,196,875.

Privacy Act Impact Assessment: No impact(s).

Nature and Extent of Confidentiality: There is no need for confidentiality with this collection of information.

Needs and Uses: Cable operators use FCC Form 1210 to file for adjustments in maximum permitted rates for regulated services to reflect external costs. Regulated cable operators submit this form to local franchising authorities.

FCC Form 1240 is filed by cable operators seeking to adjust maximum permitted rates for regulated cable services to reflect changes in external costs.

Cable operators submit Form 1240 to their respective local franchising authorities (''LFAs'') to justify rates for the basic service tier and related equipment or with the Commission (in situations where the Commission has assumed jurisdiction).

OMB Control Number: 3060–1070.

Title: Allocation and Service Rules for the 71–76 GHz, 81–86 GHz, and 92–95 GHz Bands.

Form Number: N/A.

Type of Review: Extension of a currently approved collection.

Respondents: Business or other for-profit entities; not-for-profit institutions; and State, local, or Tribal Government.

Number of Respondents: 852 respondents; 11,342 responses.

Estimated Time per Response: 0.25 to 1.5 hours.

Frequency of Response: On occasion reporting requirement, recordkeeping requirement, and third-party disclosure requirement.

Obligation to Respond: Required to obtain or retain benefits. Statutory authority for this information collection is contained in 47 U.S.C. 151, 154(i), 303(f) and (r), 309, 316, and 332 of the Communications Act of 1934, as amended.

Total Annual Burden: 12,039 hours.

Total Annual Cost: $200,000.

Privacy Impact Assessment: No impact(s).

Nature and Extent of Confidentiality: There is no need for confidentiality. The Commission has not granted assurances of confidentially to those parties submitting the information. In those cases where a respondent believes information requires confidentiality, the respondent can request confidential treatment and the Commission will afford such confidentiality for 20 days, after which the information will be available to the public.

Needs and Uses: The Commission is seeking an extension of this information collection in order to obtain the full three-year approval from OMB. There are no program changes to the reporting, recordkeeping and/or third-party disclosure requirements, but we are revising estimates based on the reduction of database managers, and the increase of renewals of the nationwide licensees. The recordkeeping, reporting, and third-party disclosure requirements will be used by the Commission to verify licensee compliance with the Commission rules and regulations, and to ensure that licensees continue to fulfill their statutory responsibilities in accordance with the Communications Act of 1934. The Commission's rules promote the private sector development and use of 71–76 GHz, 81–86 GHz, and 92–95 GHz bands (70/80/90 GHz bands). Such information has been used in the past and will continue to be used to minimize interference, verify that applicants are legally and technically qualified to hold license, and to determine compliance with Commission rules.

OMB Control Number: 3060–1272.

Title: 3.7 GHz Band Space Station Operator Accelerated Relocation Elections and Transition Plans; 3.7 GHz Band Incumbent Earth Station Lump Sum Payment Elections.

Form Number: N/A.

Type of Review: Extension of a currently approved information collection.

Respondents: Business or other for profit entities.

Number of Respondents: 3,010 respondents; 3,010 responses.

Estimated Time per Response: 16 hours per eligible space station accelerated relocation election; 80–600 hours per eligible space station transition plan; 32 hours per incumbent earth station lump sum payment election.

Frequency of Response: One-time reporting requirement.

Obligation to Respond: Required to obtain or maintain benefits. Statutory authority for this information collection is contained in sections 1, 2, 4(i), 4(j), 5(c), 201, 302, 303, 304, 307(e), and 309 of the Communications Act of 1934, as amended, 47 U.S.C. 151, 152, 154(i), 154(j), 155(c), 201, 302, 303, 304, 307(e), 309.

Total Annual Burden: 109,680 hours.

Total Annual Costs: $900,000.

Nature and Extent of Confidentiality: The information collected under this collection will be made publicly available, however, to the extent information submitted pursuant to this information collection is determined to be confidential, it will be protected by the Commission. If a respondent seeks to have information collected pursuant to this information collection withheld from public inspection, the respondent may request confidential treatment pursuant to section 0.459 of the Commission's rules for such information. See 47 CFR 0.459.

Privacy Act Impact Assessment: No impact(s).

Needs and Uses: A request for extension of this information collection (no change in requirements) will be submitted to the Office of Management and Budget (OMB) after this 60-day comment period in order to obtain the full three-year clearance from OMB. On February 28, 2020, in furtherance of the goal of releasing more mid-band spectrum into the market to support and enable next-generation wireless networks, the Commission adopted a Report and Order, FCC 20–22, (3.7 GHz Report and Order) in which it reformed the use of the 3.7–4.2 GHz band, also known as the C-Band. The 3.7–4.2 GHz band currently is allocated in the United States exclusively for non-Federal use on a primary basis for Fixed Satellite Service (FSS) and Fixed Service. Domestically, space station operators use the 3.7–4.2 GHz band to provide downlink signals of various bandwidths to licensed transmit-receive, registered receive-only, and unregistered receive-only earth stations throughout the United States. The 3.7 GHz Report and Order calls for the relocation of existing FSS operations in the band into the upper 200 megahertz of the band (4.0–4.2 GHz) and making the lower 280 megahertz (3.7–3.98 GHz) available for flexible-use throughout the contiguous United States through a Commission-administered public auction of overlay licenses in the 3.7 GHz Service that is scheduled to occur later this year, with the 20 megahertz from 3.98–4.0 GHz reserved as a guard band.

The Commission adopted a robust transition schedule to achieve an expeditious relocation of FSS operations and ensure that a significant amount of spectrum is made available quickly for next-generation wireless deployments, while also ensuring effective accommodation of relocated incumbent users. The 3.7 GHz Report and Order establishes a deadline of December 5, 2025, for full relocation to ensure that all FSS operations are cleared in a timely manner, but provides an opportunity for accelerated clearing of the band by allowing incumbent space station operators, as defined in the 3.7 GHz Report and Order, to commit to voluntarily relocate on a two-phased accelerated schedule (with additional obligations and incentives for such operators), with a Phase I deadline of December 5, 2021, and a Phase II deadline of December 5, 2023.

The Commission concluded in the 3.7 GHz Report and Order that, before the public auction of overlay licenses commences, it is appropriate for potential bidders to know when they will get access to the spectrum in the 3.7–3.98 GHz band that is currently occupied by incumbent FSS space station operators and earth stations, as defined in the 3.7 GHz Report and Order, and to have an estimate of how much they may be required to pay for incumbent relocation costs and accelerated relocation payments should they become overlay licensees, as overlay licensees are required to pay for the reasonable relocation costs of incumbent space station and incumbent earth station operators that are required to clear the lower portion of the band.

Under this information collection, the Commission will collect information that will be used by the Commission to determine when, how, and at what cost existing operations in the lower portion of the 3.7–4.2 GHz band will be relocated to the upper portion of the band. Specifically, the Commission collect the following information from incumbents as adopted in the 3.7 GHz Report and Order:

Accelerated Relocation Elections

The Commission concluded in the 3.7 GHz Report and Order that overlay licensees would only value accelerated relocation if a significant majority of incumbents are cleared in a timely manner, and therefore determined that at least 80% of accelerated relocation payments must be accepted in order for the Commission to accept accelerated elections and require overlay licensees to pay accelerated relocation payments. The 3.7 GHz Report and Order calls for an eligible space station operator, as defined in the 3.7 GHz Report and Order, that chooses to commit to clear on the accelerated schedule in exchange for accelerated relocation payments to submit a written, public, irrevocable accelerated relocation election with the Commission by May 29, 2020, to permit the Commission to determine whether there are sufficient accelerated relocation elections to trigger early relocation and in turn provide bidders with adequate certainty regarding the clearing date and payment obligations associated with each license well in advance of the auction.

Transition Plans

The 3.7 GHz Report and Order requires each eligible space station operator to submit to the Commission by June 12, 2020, and make available for public review, a detailed transition plan describing the necessary steps and estimated costs for the eligible space station operator to complete the transition of existing operations in the lower portion of the 3.7–4.2 GHz band to the upper 200 megahertz of the band and its individual timeline for doing so consistent with the regular relocation deadline or by the accelerated relocation deadlines. An eligible space station operator that elects to receive accelerated relocation payments is responsible for relocating all of its associated incumbent earth stations and must outline the details of such relocation in the transition plan (unless an incumbent earth station owner elects to receive a lump sum payment and assumes responsibility for transitioning its own earth stations). Similarly, an incumbent space station operator that does not elect to receive accelerated relocation payments but nevertheless plans to assume responsibility for relocating its own associated incumbent earth stations must make that clear in its transition plan.

Incumbent Earth Station Lump Sum Payment Elections

The 3.7 GHz Report and Order provides an incumbent earth station operator with the option of accepting reimbursement payments for its reasonable relocation costs for the transition, or opting out of the formal relocation process and accepting a lump sum reimbursement payment for all of its incumbent earth stations based on the average, estimated costs of relocating all of their incumbent earth stations in lieu of actual relocation costs. The 3.7 GHz Report and Order directs the Wireless Telecommunications Bureau to announce the lump sum that will be available per incumbent earth station as well as the process for electing lump sum payments and requires that no later than 30 days after this announcement, an incumbent earth station operator that wishes to receive a lump sum payment make an irrevocable lump sum payment election that will apply to all of its earth stations in the contiguous United States.

This information collection will serve as the starting point for planning and managing the process of efficiently and expeditiously clearing of the lower portion of the band, so that this spectrum can be auctioned for flexible-use service licenses.

Federal Communications Commission.

Marlene Dortch,

Secretary, Office of the Secretary.

[FR Doc. 2020–20113 Filed 9–11–20; 8:45 am]

BILLING CODE 6712–01–P

FEDERAL COMMUNICATIONS COMMISSION

[OMB 3060–0791; FRS 17062]

Information Collection Being Reviewed by the Federal Communications Commission Under Delegated Authority

AGENCY: Federal Communications Commission.

ACTION: Notice and request for comments.

SUMMARY: As part of its continuing effort to reduce paperwork burdens, and as required by the Paperwork Reduction Act (PRA) of 1995, the Federal Communications Commission (FCC or the Commission) invites the general public and other Federal agencies to take this opportunity to comment on the following information collection. Comments are requested concerning: Whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; the accuracy of the Commission's burden estimate; ways to enhance the quality, utility, and clarity of the information collected; ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology; and ways to further reduce the information collection burden on small business concerns with fewer than 25 employees. The FCC may not conduct or sponsor a collection of information unless it displays a currently valid control number. No person shall be subject to any penalty for failing to comply with a collection of information subject to the PRA that does not display a valid Office of Management and Budget (OMB) control number.

DATES: Written PRA comments should be submitted on or before November 13, 2020. If you anticipate that you will be submitting comments, but find it difficult to do so within the period of time allowed by this notice, you should advise the contact listed below as soon as possible.

ADDRESSES: Direct all PRA comments to Nicole Ongele, FCC, via email *PRA@fcc.gov* and to *Nicole.Ongele@fcc.gov.*

FOR FURTHER INFORMATION CONTACT: For additional information about the information collection, contact Nicole Ongele at (202) 418–2991.

SUPPLEMENTARY INFORMATION:

OMB Control Number: 3060–0791.

Title: Section 32.7300, Accounting for Judgments and Other Costs Associated with Litigation.

Form Number: N/A.

Type of Review: Extension of a currently approved collection.

Respondents: Business or other for-profit.

Number of Respondents and Responses: 2 respondents; 2 responses.

Estimated Time per Response: 4–36 hours.

Frequency of Response: On occasion reporting requirement and recordkeeping requirement.

Obligation to Respond: Required to obtain or retain benefits. Statutory authority for this collection of information is contained in 47 U.S.C. 151, 152, 154, 161, 201–205 and 218–220 of the Communications Act of 1934, as amended.

Total Annual Burden: 40 hours.

Total Annual Cost: No cost.

Privacy Act Impact Assessment: No impact(s).

Nature and Extent of Confidentiality: There is no need for confidentiality. The Commission is not requesting that respondents submit confidential information to the FCC.

Needs and Uses: The Commission is seeking Office of Management and Budget (OMB) approval for an extension of this information collection (no change in the reporting and/or recordkeeping requirements). The Commission will submit this information collection after this 60-day comment period to the OMB. The Commission adopted accounting rules that require carriers to account for adverse federal antitrust judgments and post-judgment special charges. With regard to settlements of such lawsuits, there will be a presumption that carriers can recover the portion of the settlement that represents the avoidable costs of litigation; provided that the carrier makes a required showing. To receive recognition of its avoided cost of litigation a carrier must demonstrate, in a request for special relief, the avoided costs of litigation by showing the amount corresponding to the additional litigation expenses discounted to present value, that the carrier reasonably estimates it would have paid if it had not settled. Settlement costs in excess of the avoided costs of litigation are presumed not recoverable unless a carrier rebuts that presumption by showing the basic factors that enticed the carrier to settle and demonstrating that ratepayers benefited from the settlement.

Federal Communications Commission.

Marlene Dortch,

Secretary, Office of the Secretary.

[FR Doc. 2020–20101 Filed 9–11–20; 8:45 am]

BILLING CODE 6712–01–P

FEDERAL COMMUNICATIONS COMMISSION

[OMB 3060–0297; FRS 17061]

Information Collection Being Reviewed by the Federal Communications Commission Under Delegated Authority

AGENCY: Federal Communications Commission.

ACTION: Notice; request for comments.

SUMMARY: As part of its continuing effort to reduce paperwork burdens, and as required by the Paperwork Reduction Act (PRA), the Federal Communications Commission (FCC or Commission) invites the general public and other Federal agencies to take this opportunity to comment on the following information collections. Comments are requested concerning: Whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; the accuracy of the Commission's burden estimate; ways to enhance the quality, utility, and clarity of the information collected; ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology; and ways to further reduce the information collection burden on small business concerns with fewer than 25 employees.

DATES: Written comments should be submitted on or before November 13, 2020. If you anticipate that you will be submitting comments, but find it difficult to do so within the period of time allowed by this notice, you should advise the contacts below as soon as possible.

ADDRESSES: Direct all PRA comments to Cathy Williams, FCC, via email *PRA@fcc.gov* and to *Cathy.Williams@fcc.gov.*

FOR FURTHER INFORMATION CONTACT: For additional information about the information collection, contact Cathy Williams at (202) 418–2918.

SUPPLEMENTARY INFORMATION: The FCC may not conduct or sponsor a collection of information unless it displays a currently valid Office of Management and Budget (OMB) control number. No person shall be subject to any penalty for failing to comply with a collection of information subject to the PRA that does not display a valid OMB control number.

As part of its continuing effort to reduce paperwork burdens, and as required by the PRA of 1995 (44 U.S.C. 3501–3520), the FCC invites the general public and other Federal agencies to take this opportunity to comment on the following information collections. Comments are requested concerning: Whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; the accuracy of the Commission's burden estimate; ways to enhance the quality, utility, and clarity of the information collected; ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology; and ways to further reduce the information collection burden on small business concerns with fewer than 25 employees.

OMB Control Number: 3060–0297.

Title: Section 80.503, Cooperative Use of Facilities.

Form Number: N/A.

Type of Review: Extension of a currently approved collection.

Respondents: Business or other for-profit entities; Not-for-profit institutions; and State, Local, or Tribal Government.

Number of Respondents: 100 respondents; 100 responses.

Estimated Time per Response: 16 hours.

Frequency of Response: Occasion reporting requirement and Recordkeeping requirement.

Obligation to Respond: Required to obtain or retain benefits. Statutory authority for this information collection is contained in 47 U.S.C. Sections 151–155, 301–609 of the Communications Act of 1934, as amended; and 3 UST 3450, 3 UST 4726, 12 UST 2377.

Total Annual Burden: 1,600 hours.

Total Annual Cost: No cost.

Privacy Impact Assessment: No impact(s).

Needs and Uses: The information collection requirements contained in Section 80.503 require that a licensee of a private coast station or marine utility station on shore may install ship radio stations on board United States commercial transport vessels of other persons. In each case these persons must enter into a written agreement verifying that the ship station licensee has the sole right of control of the ship stations, that the vessel operators must use the ship stations subject to the orders and instructions of the coast station or marine utility station on shore, and that the ship station licensee will have sufficient control of the ship station to enable it to carry out its responsibilities under the ship station license. A copy of the contract/written agreement must be kept with the station records and made available for inspection by Commission representatives.

The information is used by FCC personnel during inspection and investigations to ensure compliance with applicable rules. If this information was not available, enforcement efforts could be hindered; frequency congestion in certain bands could increase; and the financial viability of some public coast radiotelephone stations could be threatened.

Federal Communications Commission.

Marlene Dortch,

Secretary.

[FR Doc. 2020–20112 Filed 9–11–20; 8:45 am]

BILLING CODE 6712–01–P

FEDERAL MEDIATION AND CONCILIATION SERVICE

[Docket No.: FMCS–2020–0003–0001]

Notice for a Collaboration Between Universities and the FMCS

AGENCY: Office of the Director (OD), Federal Mediation and Conciliation Service (FMCS).

ACTION: Final action.

SUMMARY: As a policy initiative, FMCS is collaborating with colleges and universities to exchange alternative dispute resolution research and techniques.

DATES: Effective 30 days after publication.

ADDRESSES: Inquiries can be sent by email to *scudahy@fmcs.gov;* the address for personal or postal delivery is Office of the General Counsel, FMCS, Floor 7, One Independence Square, 250 E St. SW, Washington, DC, 20427. Please note that as of September 9, 2020, the FMCS office is not open for visitors and mail is not checked daily. Therefore, we encourage emailed inquiries.

FOR FURTHER INFORMATION CONTACT: For specific questions related to this program, please contact Sarah Cudahy, 202–606–8090, *scudahy@fmcs.gov.*

SUPPLEMENTARY INFORMATION: No comments were received during the comment period. 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 FMCS–2020–0003–0001.

Dated: September 9, 2020.

Sarah Cudahy,

General Counsel.

[FR Doc. 2020–20177 Filed 9–11–20; 8:45 am]

BILLING CODE 6732–01–P

FEDERAL MEDIATION AND CONCILIATION SERVICE

[Docket No.: FMCS–2020–0004–0001]

Student Award Program Announcement

AGENCY: Office of the Director (OD), Federal Mediation and Conciliation Service (FMCS).

ACTION: Final action.

SUMMARY: As a policy initiative, FMCS has created a student award program.

DATES: Effective 30 days after publication.

ADDRESSES: Inquiries can be sent by email to *scudahy@fmcs.gov;* the address for personal or postal delivery is Office of the General Counsel, FMCS, Floor 7, One Independence Square, 250 E. St. SW, Washington, DC, 20427. Please note that as of September 9, 2020, the FMCS office is not open for visitors and mail is not checked daily. Therefore, we encourage emailed inquiries.

FOR FURTHER INFORMATION CONTACT: For specific questions related to this program, please contact Sarah Cudahy, 202–606–8090.

SUPPLEMENTARY INFORMATION: No comments were received during the comment period. 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 FMCS–2020–0004–0001.

Dated: September 9, 2020.

Sarah Cudahy,

General Counsel.

[FR Doc. 2020–20174 Filed 9–11–20; 8:45 am]

BILLING CODE 6732–01–P

FEDERAL RESERVE SYSTEM

Agency Information Collection Activities: Announcement of Board Approval Under Delegated Authority and Submission to OMB

AGENCY: Board of Governors of the Federal Reserve System.

ACTION: Approval of information collection.

SUMMARY: The Board of Governors of the Federal Reserve System (Board) has adopted a proposal to extend for three years, with revision, the Capital Assessments and Stress Testing Reports (FR Y–14A/Q/M; OMB No. 7100–0341). The revisions are applicable with as of dates ranging from September 30, 2020, to June 30, 2021.

FOR FURTHER INFORMATION CONTACT: Federal Reserve Board Clearance Officer—Nuha Elmaghrabi—Office of the Chief Data Officer, Board of Governors of the Federal Reserve System, Washington, DC 20551, (202) 452–3829.

Office of Management and Budget (OMB) Desk Officer—Shagufta Ahmed—Office of Information and Regulatory Affairs, Office of Management and Budget, New Executive Office Building, Room 10235, 725 17th Street NW, Washington, DC 20503, or by fax to (202) 395–6974.

A copy of the Paperwork Reduction Act (PRA) OMB submission, including the reporting form and instructions, supporting statement, and other documentation will be placed into OMB's public docket files. These documents also are available on the Federal Reserve Board's public website at *https://www.federalreserve.gov/apps/reportforms/review.aspx* or may be requested from the agency clearance officer, whose name appears above.

SUPPLEMENTARY INFORMATION: On June 15, 1984, OMB delegated to the Board authority under the PRA to approve and assign OMB control numbers to collections of information conducted or sponsored by the Board. Board-approved collections of information are incorporated into the official OMB inventory of currently approved collections of information. Copies of the PRA Submission, supporting statements, and approved collection of information instrument(s) are placed into OMB's public docket files.

Final Approval Under OMB Delegated Authority of the Extension for Three Years, With Revision, of the Following Information Collection

Report title: Capital Assessments and Stress Testing Reports.

Agency form number: FR Y–14A/Q/M.

OMB control number: 7100–0341.

Frequency: Annually, quarterly, and monthly.

Respondents: These collections of information are applicable to bank holding companies (BHCs), U.S. intermediate holding companies (IHCs), and savings and loan holding companies (SLHCs)[1] with $100 billion or more in total consolidated assets, as based on: (i) The average of the firm's total consolidated assets in the four most recent quarters as reported quarterly on the firm's Consolidated Financial Statements for Holding Companies (FR Y–9C); or (ii) if the firm has not filed an FR Y–9C for each of the most recent four quarters, then the average of the firm's total consolidated assets in the most recent consecutive quarters as reported quarterly on the firm's FR Y–9Cs. Reporting is required as of the first day of the quarter immediately following the quarter in which the respondent meets this asset threshold, unless otherwise directed by the Board.

Estimated number of respondents: FR Y–14A/Q: 36; FR Y–14M: 34.[2]

Estimated average hours per response: FR Y–14A: 926 hours; FR Y–14Q: 2,201 hours; FR Y–14M: 1,072 hours; FR Y–14 On-going Automation Revisions: 480 hours; FR Y–14 Attestation On-going Attestation: 2,560 hours.

Estimated annual burden hours: FR Y–14A: 33,336 hours; FR Y–14Q: 316,944 hours; FR Y–14M: 437,376 hours; FR Y–14 On-going Automation Revisions: 17,280 hours; FR Y–14 Attestation On-going Attestation: 33,280 hours.

General description of report: This family of information collections is composed of the following three reports:

- The FR Y–14A collects quantitative projections of balance sheet, income, losses, and capital across a range of macroeconomic scenarios and qualitative information on methodologies used to develop internal projections of capital across scenarios.[3]
- The quarterly FR Y–14Q collects granular data on various asset classes, including loans, securities, trading assets, and PPNR for the reporting period.
- The monthly FR Y–14M is comprised of three retail portfolio- and loan-level schedules, and one detailed address-matching schedule to supplement two of the portfolio and loan-level schedules.

The data collected through the FR Y–14A/Q/M reports (FR Y–14 reports) provide the Board with the information needed to help ensure that large firms have strong, firm-wide risk measurement and management processes supporting their internal assessments of capital adequacy and that their capital resources are sufficient given their business focus, activities, and resulting risk exposures. The reports are used to support the Board's annual Comprehensive Capital Analysis and Review (CCAR) and Dodd-Frank Act Stress Test (DFAST) exercises, which complement other Board supervisory efforts aimed at enhancing the continued viability of large firms, including continuous monitoring of firms' planning and management of liquidity and funding resources, as well as regular assessments of credit, market and operational risks, and associated risk management practices. Information gathered in this data collection is also used in the supervision and regulation of respondent financial institutions. Respondent firms are currently required to complete and submit up to 17 filings each year: one annual FR Y–14A filing, four quarterly FR Y–14Q filings, and 12 monthly FR Y–14M filings. Compliance with the information collection is mandatory.

Current actions: On March 19, 2020, the Board published a notice in the **Federal Register** (85 FR 15776) requesting public comment for 60 days on the extension, with revision, of the FR Y–14 reports. The proposed revisions consisted of changes necessary to better identify risk as part of the stress tests, such as revisions related to wholesale, trading, and counterparty exposures, as well as capital revisions related to capital simplification, total loss-absorbing capacity (TLAC), and the standardized approach for counterparty credit risk (SA–CCR). The Board also proposed to make several clarifications to the instructions that were, in part, prompted by questions the Board had received from reporting institutions. The comment period for this notice expired on May 18, 2020. The Board

[1] SLHCs with $100 billion or more in total consolidated assets become members of the FR Y–14Q and FR Y–14M panels effective June 30, 2020, and the FR Y–14A panel effective December 31, 2020. *See* 84 FR 59032 (November 1, 2019).

[2] The estimated number of respondents for the FR Y–14M is lower than for the FR Y–14Q and FR Y–14A because, in recent years, certain respondents to the FR Y–14A and FR Y–14Q have not met the materiality thresholds to report the FR Y–14M due to their lack of mortgage and credit activities. The Board expects this situation to continue for the foreseeable future.

[3] On October 10, 2019, the Board issued a final rule that eliminated the requirement for firms subject to Category IV standards to conduct and publicly disclose the results of a company-run stress test. See 84 FR 59032 (Nov. 1, 2019). That final rule maintained the existing FR Y–14 substantive reporting requirements for these firms in order to provide the Board with the data it needs to conduct supervisory stress testing and inform the Board's ongoing monitoring and supervision of its supervised firms. However, as noted in the final rule, the Board intends to provide greater flexibility to banking organizations subject to Category IV standards in developing their annual capital plans and consider further change to the FR Y–14 forms as part of a separate proposal. See 84 FR 59032, 59063.

received two comment letters from banking organizations and one comment letter from a banking industry group. The Board has adopted the proposed revisions, except as discussed below. In addition, although the Board did not receive any comment letters regarding the proposed revisions related to a proposed rule that would modify the Board's TLAC requirements,[4] the Board has not adopted these revisions as proposed. Instead, the Board would address these revisions at such point as the Board adopts a final rule.

Detailed Discussion of Public Comments

Capital Simplifications

The Board proposed to revise the FR Y–14 reports to incorporate the changes finalized by the agencies that amended their regulatory capital rules (simplifications rule).[5] [6] The Board proposed these revisions to be effective for the September 30, 2020, FR Y–14Q submission and for the December 31, 2020, FR Y–14A submission. In the simplifications rule, the agencies adopted a simpler methodology for non-advanced approaches banking organizations [7] to calculate minority interest limitations and simplified the regulatory capital treatment of mortgage service assets (MSAs), temporary difference deferred tax assets (DTAs), and investments in the capital of unconsolidated financial institutions for non-advanced approaches banking organizations. The simplifications rule became effective April 1, 2020.[8]

The Board received two comments on the proposed changes to the FR Y–14 reports related to the simplifications rule. First, a banking organization asked why the timing of the capital simplifications-related proposed revisions to the FR Y–14Q report did not align with the timing of similar revisions made to the FR Y–9C, which were effective for the March 31, 2020, as of date.[9] The same banking organization also asked whether firms could early adopt the capital simplifications revisions for FR Y–14Q reporting before the proposed effective dates.

In order to allow firms to incorporate the effects of the capital simplifications rule into the FR Y–14Q report, the Board would have needed to add items to Schedule D (Regulatory Capital), which it proposed to do. It was not possible to allow eligible firms to incorporate the effects of the capital simplifications rule before the proposed effective date of September 30, 2020, without temporarily revising the FR Y–14Q. Firms will have to wait until the September 30, 2020, FR Y–14Q submission, to be able to incorporate these effects, and firms do not have the option to early adopt for FR Y–14Q reporting purposes. It is important to note that this does not inhibit eligible firms from taking advantage of the capital simplifications rule for purposes of capital adequacy compliance through other reports, such as the FR Y–9C.

Counterparty

Client-Cleared Derivatives

The Board proposed to require all client-cleared derivatives exposures to be reported on the large counterparty default (LCPD) section of FR Y–14Q, Schedule L (Counterparty), effective beginning September 30, 2020. One commenter was not supportive of this revision, as it commented that firms do not have this information readily available. Per the commenter, it would be operationally burdensome for firms to gather information related to client-cleared derivatives, especially given the volume of reported data that this revision would add to Schedule L. The commenter suggested that if the Board were to adopt this revision as proposed, then the Board should delay the effective until June 30, 2021.

The Board acknowledges the operational concerns raised by the industry, especially given the timing of the coronavirus disease 2019 (COVID–19) pandemic. The Board has adopted this revision as proposed, except that it has delayed the effective date until June 30, 2021. In fact, due to the operational concerns raised by the industry and the timing of the COVID–19 pandemic, the Board has delayed the effective date for all FR Y–14Q, Schedule L revisions until June 30, 2021.

The same commenter further stated that this revision would require firms to report exposures of their clients, and not exposures of the banks themselves. Per the comment, this goes against the spirit of the data collection, which is to capture reporting firm exposures.

The Board notes that, per the draft instructions, the requirement for a firm to report its exposures to clients (*i.e.,* member to client leg) applies only when the firm has credit exposures to a client, either directly (*i.e.,* the case in which the firm is acting as a financial intermediary on behalf of the client and enters into an offsetting transaction with a central counterparty (CCP) or an exchange (referred to as a back-to-back derivative)), or indirectly (*i.e.,* the case in which the firm guarantees the client's performance to a CCP or an exchange (referred to as a guaranteed derivative)). Further, a firm's reporting requirement associated with its client-cleared exposures to CCPs (*i.e.,* member to CCP leg) applies only when the firm has a credit exposure to a CCP, that is, either directly (*i.e.,* the case of a back-to-back derivative) or indirectly (*i.e.,* the case in which the firm guarantees the performance of the CCP or exchange to the client). Therefore, firms are only required to report client-clearing derivative exposures in instances where firms are directly or indirectly exposed. For these reasons, the Board has adopted this revision as proposed, except that has delayed the effective date until June 30, 2021.

The commenter also expressed concern that it is not clear on which portions of Schedule L client-cleared derivatives exposures information should be reported. Per the comment, the initial notice used the phrase ''large counterparty default'' section and the draft instructions provided with the initial notice did not specify where these exposures should be reported.

Per the proposal, client-cleared derivatives exposures information would be reported in Schedule L.5 (Derivatives and Securities Financing Transactions (SFT) Profile). The Board has adopted this revision as proposed, except that has delayed the effective date until June 30, 2021.

The Board specified in the initial notice that it was only going to collect information on client-cleared derivative exposures for monitoring purposes, and not for use in the stress test at this time. Per the commenter, the draft instructions provided with the initial notice did not make it clear how client-cleared derivative exposures would be delineated from other exposures to ensure they would not be included in the stress test at this time.

The Board will be able to delineate client-cleared derivative exposures from other exposures using the ''Agreement Role'' item of Schedule L.5.1 (Derivative and SFT information by counterparty legal entity and netting set/agreement). The ''Agreement Role'' item provides

[4] *See* 84 FR 13814 (April 8, 2019).

[5] *See* 12 CFR part 3 (OCC); 12 CFR part 217 (Board); 12 CFR part 324 (FDIC). While the agencies have codified the capital rule in different parts of title 12 of the Code of Federal Regulations, the internal structure of the sections within each agency's rule is substantially similar. All references to sections in the capital rule or the proposal are intended to refer to the corresponding sections in the capital rule of each agency.

[6] *See* 84 FR 35234 (July 22, 2019).

[7] Non-advanced approaches banking organizations are institutions that do not meet the criteria in 12 CFR 3.100(b) (OCC); 12 CFR 217.100(b) (Board); or 12 CFR 324.100(b) (FDIC).

[8] Eligible firms could have chosen to adopt the simplifications rule effective January 1, 2020.

[9] *See* 85 FR 18230 (April 1, 2020).

the firm with a means to report its cleared derivative exposures to a client in a manner that may be distinguished from the firm's other bilateral derivative exposures to the client. The Board has adopted this revision as proposed, except that has delayed the effective date until June 30, 2021.

Netting Agreement Reporting

The Board proposed to revise the FR Y–14Q, Schedule L instructions to provide illustrative examples that clarify netting agreement reporting requirements, including describing when firms should report mark-to-market (MtM) amounts with a counterparty on a gross or net basis. One commenter indicated that under U.S. Generally Accepted Accounting Principles (GAAP), firms are not permitted to offset negative and positive MtM with the same counterparty in the absence of a legally enforceable netting agreement. Per the commenter, the proposed reporting of netting requirements would go against U.S. GAAP. The commenter recommended that the Board permit firms to report positive and negative MtM amounts with a counterparty on a gross basis without offsetting in the absence of a legally enforceable netting agreement between the firm and the counterparty.

While the proposed change to the netting agreement reporting section in Schedule L.5 reiterated the existing language in other parts of the instructions pertaining to Net Current Exposure (CE) and Mark-to-Market (MtM) items, the Board acknowledges the point raised by the commenter concerning the importance of consistency between FR Y–14 reporting and U.S. GAAP, where possible. To that end, the Board has modified the instructions so that firms are required to report MtM amounts with a counterparty on a gross basis without offsetting positive and negative MtM amounts in cases where there is no legally enforceable netting agreement. In essence, the netting rule should apply consistently between MtM and Net CE even when there is no netting agreement in place, or when a netting agreement exists but that is not legally enforceable, so that both data fields are computed after aggregating across positions that have positive MtM amounts, without allowing any offset against negative MtM amounts.

The same commenter also asked the Board to provide additional examples regarding netting agreement reporting provided in the draft instructions to better illustrate how firms should report when both positive and non-positive legal opinions exist for a given netting agreement. Specifically, the commenter recommended that the Board clarify how values should be reported if there are both positive and negative legal opinions on collateral enforceability for a netting agreement.

The Board strives to clarify the instructions to ensure accurate reporting where possible, and has revised the instructions to state that in cases where mixed legal opinions exist for either a netting agreement or a collateral enforceability, firms should apply the methodologies that are consistent with the treatment for the regulatory capital rules, and report applicable data fields accordingly.

A commenter recommended that the Board include instructions on what agreement type value should be reported in cases where there is both SFT and derivatives exposure but not cross product netting. Additionally, the commenter recommended that the Board clarify what value of agreement type should be included if there is no netting agreement for SFT and derivatives between CCP and non-CCP.

In order to remove ambiguity, the Board has revised the instructions so that firms may report ''Other'' under ''Agreement Type'' in cases where the allowable entries currently listed in the instructions do not represent the characteristics of the exposure being reported.

A commenter asked the Board to clarify how to aggregate contractual terms from credit support annexes (CSAs). Per the commenter, firms currently report at the margin level, while the proposed instructions would require firms to report at netting agreement level.

For clarity, the Board has revised the instructions so that firms may report certain margin agreement details (such as agreement type, CSA contractual features, non-cash collateral type, threshold, minimum transfer amount CP, margin frequency, etc.) at a margin agreement level in cases where multiple CSAs with different contractual features per netting agreement exist. When doing so, firms are required to use the ''Netting Set ID'' naming convention in a manner that is a concatenation of a unique identifier assigned to a netting agreement and that to a margin agreement.

A commenter further requested that the Board provide clarification regarding reporting granularity of counterparty and netting, as these concepts differ between Schedules L.1 and L.5.

The Board notes that the level of granularity of counterparty and netting intentionally differs between Schedules L.1 and L.5. Consistent with the proposed instructions, firms should report Schedules L.1–L.3 at the counterparty legal entity level and Schedule L.5 at the netting set level. The Board has adopted the revision as proposed, except that has delayed the effective date until June 30, 2021.

CDS Hedge Notional

The Board proposed several revisions to the instructions surrounding the ''CDS Hedge Notional'' item on FR Y–14Q, Schedule L.5.1, such as clarifying that when firms are calculating the net notional amount, purchased CDS hedge notional amounts must be reflected as negative amounts and sold amounts must be reflected as positive amounts. A commenter stated that the concept of CDS hedges appears also appears on Schedule L.1, and the definitions are not consistent between Schedule L.1 and Schedule L.5.1.

The Board notes that the scope of CDS hedge positions in Schedule L.1 intentionally differs from that of Schedule L.5.1. Consistent with the instructions, the ''Single Name Credit Hedges'' item in Schedule L.1 is limited to single name CDS only, whereas the ''CDS Hedge Notional'' item in Schedule L.5.1 covers a range of positions that are eligible credit derivatives as defined in 12 CFR 252.71. The Board has adopted the revisions as proposed, except that has delayed the effective date until June 30, 2021.

Variation Margins

The Board proposed to align the FR Y–14Q, Schedule L instructions regarding how variation margins can be treated with the guidance provided in SR Letter 17–7 (Regulatory Capital Treatment of Certain Centrally-cleared Derivative Contracts under the Board's Capital Rule).[10] The commenter asked to confirm whether this guidance could be interpreted as requiring firms to report zero in the variation margin column for exposures to CCPs, whose rulebook considers variation margin as a settlement payment. In addition, the commenter asked the Board to confirm whether variation margin should be included in the Gross CE column of Schedule L and whether firms should continue to report all exposures to the CCP, such as default fund contributions and initial margin and any other collateral provided to the CCP that exceeds contract MtM amounts in their specific columns.

The Board confirms that the commenter's interpretation of SR 17–7

[10] *https://www.federalreserve.gov/supervisionreg/srletters/sr1707a1.pdf.*

is appropriate for the Schedule L reporting purposes, and has adopted the revision as proposed, except that has delayed the effective date until June 30, 2021.

Trading

Formalizing Supplemental Collections

The Board proposed to formalize two supplemental collections by incorporating them into FR Y–14Q, Schedule F (Trading). One of these supplemental collections would require firms to report corporate single name exposures at the obligor level in Schedule F.22 ([Incremental Default Risk] IDR—Corporate Credit) along with corporate index exposures at the series level.

A commenter stated that requiring firms to report corporate single name exposures at the obligor level, as well as corporate index exposures at the series level, would result in significant operational challenges, as this level of data is not readily available in firms' internal systems. Per the commenter, the supplemental collection on which this proposal was based was only collected annually, and so the data was aggregated manually by firms. Since the proposal would have required that this information be provided on a quarterly basis, firms would have needed to develop a systemic solution, which would take time to implement. Therefore, the commenter recommended that this revision be delayed until June 30, 2021. The commenter also recommended that the Board clarify the definition of ''average credit spread'' in the instructions for Schedule F.22.

The Board acknowledges the operational concerns raised by the industry, especially given the timing of the COVID–19 pandemic. In light of these concerns, the Board has adopted the requirements to report corporate single name exposures at the obligor level and to report corporate index exposures at the series level as proposed, except that the Board has delayed the effective date of this revision until June 30, 2021. In addition, Board has revised the instructions for Schedule F.22 to specify that the ''average credit spread'' should be calculated using a standardized 5-year tenor.

Hedge Reporting

The Board proposed to require firms to report a version of FR Y–14Q, Schedule F that captures the impact of accrual loan hedges. A commenter indicated that it would be operationally burdensome to submit data on accrual loan hedges on a quarterly basis, as controls and verification for this data need to be set up. The commenter further stated that for some firms, hedges are generally utilized to cover credit risk without regard for how the underlying loan is accounted. Therefore, in order to comply with the proposed revisions related to accrual loan hedges, such firms would need to isolate hedges based on accounting treatment of their underlying loan risk. Per the commenter, separating this data would pose a significant burden for such firms, and would require them to invest additional time and resources in FR Y–14 reporting. Given this, the commenter recommended that this revision be postponed until June 30, 2021.

The Board acknowledges the operational concerns raised by the industry, especially given the timing of the COVID–19 pandemic. In light of these concerns, the Board has adopted the requirement to separately report accrual loan hedges as proposed, except that the Board has delayed the effective date of this revision until June 30, 2021.

The Board proposed to add the following language to the Schedule F instructions: ''Positions that are held outside of the trading book that are hedges of accrual loans or hedges of loans held under fair value accounting (FVO hedges) should not be included in this schedule. Instead, they should each be reported separately in their own FR Y–14Q Trading schedules.'' A commenter asked the Board to specify to which ''positions'' these instructions refer, and to clarify the reporting requirements for such positions.

To minimize ambiguity, the Board has clarified that the phrase ''outside the trading book'' refers to positions reported outside of FR Y–9C, Schedule HC–D (Trading Assets and Liabilities). Reporting locations for such positions include, for example, FR Y–9C, Schedules HC–F (Other Assets) and HC–G (Other Liabilities).

Further, the Board has revised the instructions to make it clear that positions hedging FVO loans should be reported with submission type ''FVO Hedges'' and positions hedging accrual loans should be reported with submission type ''Accrual Loan Hedges.''

The Board proposed revisions related to hedge reporting on FR Y–14Q, Schedule F in order to isolate the impact of specific hedges (*e.g.,* X-valuation adjustment or XVA hedges). Specifically, the Board proposed to revise the instructions to clarify that XVA hedges should not be reported on Schedule F. A commenter stated that not requiring XVA hedges to be reported on Schedule F would be challenging for firms, as these hedges are built into pricing models when re-valuing positions under the global market shock. Further, per the commenter, these hedges are critical for reporting the impact for private equity exposures. The commenter stated that adopting these revisions as proposed would require significant modeling changes, which would create operational burden in terms of testing and validating results. Therefore, the commenter recommended that this revision be delayed until June 30, 2021.

The Board acknowledges the changes required for firms to comply with this proposed revision. Given these challenges and the timing of the COVID–19 pandemic, the Board has adopted the revision as proposed, except that it has delayed the effective date until June 30, 2021.

Wholesale

Undrawn Commitments

The Board proposed to revise the FR Y–14Q, Schedule H (Wholesale) to require firms to report interest rate data for undrawn commitments as if they were fully drawn on the reporting date. A commenter stated that the Board should not adopt this revision, as most firms do not have systems in place to capture interest rate information on undrawn commitments. Per the commenter, gathering and vetting this information would require significant manual review of physical documents.

The Board needs interest rate information for undrawn exposures to more accurately estimate wholesale risk and potential credit availability in a stressed environment, as interest rate information provides a measure of risk that is quantitative and uniformly defined across reporting entities. However, due to the challenges associated with adopting this revision, as well as the timing of the COVID–19 pandemic, the Board has delayed the effective date for this revision until December 31, 2020.

Two commenters stated that in many cases, there are multiple interest rate options available for an undrawn commitment and the borrower is not required to choose an interest rate until a draw has been made. The commenters also requested that the Board clarify how the interest rate should be reported for variable rate loans, credit facilities with loans with varying interest rates, loans with multiple rate reset scenarios, and interest rates based on performance metrics. The Board proposed instructions that would have required firms to report the most conservative interest rate allowed per the terms of the credit agreement if a credit facility allows for multiple interest rates. Per one of the commenters, requiring the most conservative rate would need to be recalculated for each report date, which would require significant resources.

To reduce the unintended burden of recalculating the most conservative interest rate each quarter, the Board has revised the language regarding which interest rate to report for facilities with multiple interest rate options to specify that firms should report the most conservative (highest) rate as of the most recent of origination or renewal date. The Board has revised the instructions to further clarify that in cases when the facility is an acquired facility and acquired more recently than origination or renewal, the reported rate should be the most conservative at time of acquisition. This revised language allows for consistent reporting over time of the combination of options that comprise an interest rate for an undrawn facility. For example, assuming at origination, a London Inter-Bank Offered Rate (LIBOR) index plus spread amounts to a 4.25% interest rate, and a Base index plus spread amounts to a 4.50% interest rate, the interest rate reported would be the Base index plus spread for each subsequent reporting period that the origination or renewal date does not change and the facility remains fully undrawn. The same logic should be applied to other scenarios that allow for multiple interest rates.

A commenter stated that there was the need for further clarification in order to properly calculate interest rates for undrawn commitments, such as in situations where the date used to calculate the interest rate is a different date than the draw date.

To remove ambiguity, the Board has clarified the instructions to state that the funding date should be considered the reporting date.

Legal Entity Identifiers

The Board proposed to require firms to report Legal Entity Identifiers (LEIs) assigned to obligors and if applicable, entities that are identified as the primary source or repayment when the primary source of repayment differs from the reported obligor, for credit facilities reported on Schedule H. A commenter indicated that many firms do not collect LEI information from their clients and there is no automated way to gather or validate LEI data. Per the commenter, firms do not currently have systems in place to maintain LEI information and small naming differences or misspellings can lead to LEI mismatches. Therefore, requiring LEIs would require costly system updates and significant resources to accurately report.

The commenter further added that requiring LEIs at any time would be challenging, but given the outbreak of the COVID–19 pandemic, firms do not have ample resources to dedicate to system changes associated with LEIs. The commenter recommended that if the Board adopts this proposal, then it should delay this requirement until after the COVID–19 pandemic has subsided.

The Board believes there is a significant benefit to using LEI data to identify obligors, as it is globally available and contains information about entity structure. This makes it a beneficial addition to the other identifiers collected in the Schedule H, and the trend is toward using LEI data. However, the Board acknowledges that firms will need time to capture the LEI data for their obligors, especially given the timing of the COVID–19 pandemic. Accordingly, the Board has adopted this revision as proposed, except that it has delayed the effective date of this revision until June 30, 2021.

Property Size

The Board proposed to revise FR Y–14Q, Schedule H.2 (Commercial Real Estate), item 39 (''Property Size'') to clarify that predominance can be used to determine the units even if the loan consists of mixed property types. A commenter stated that this revision inadvertently creates ambiguity as it would no longer be clear when the ''Other'' option for item 39 would be used. The commenter further stated that the proposed revision would not clearly address the reporting of mixed property types, as it would still be unclear if firms are to only report the size of the single predominate property type and exclude the size of the other property types that secure the facility. For these reasons, the commenter suggested not adopting the proposed revisions.

The Board believes the proposed clarifications remain necessary as they address an ambiguity in the instructions concerning how to report property size when there is a single property with multiple property types where one property type predominates. To provide greater clarity, the Board has revised the instructions for item 39 to indicate the reporting of property size when the option reported in Schedule H.2, item 9 (''Property Type'') is ''Other''. The Board has also revised the instructions to state that the reported property size should be based on the size of the entire property.

Capital Call Subscriptions

The Board proposed to add options of ''Revolving Credit (of any type)—Capital Call Subscription'' and ''Term loan (of any type)—Capital Call Subscription'' to FR Y–14Q, Schedule H.1, item 20 (''Credit Facility Type''). The Board also proposed to add the option of ''Capital Call Subscription'' to item 22 (''Credit Facility Purpose''). A commenter indicated that the Board should not adopt the revisions to item 20, as the Board could combine the values reported in items 20 and 22 to identify revolving credit and term loans that are capital call subscriptions.

The Board agrees with the commenter that the revisions as proposed are duplicative. As a result, the Board has not adopted the proposed revisions to the instructions for Schedule H.1, item 20 (''Credit Facility Type''). However, the Board has adopted the revisions as proposed to Schedule H.1 (Corporate Loan), item 22 (''Credit Facility Purpose''), so that the Board can still identify capital call subscriptions.

Retail

Credit Cards

The Board proposed to revise items 11 (''Projected Managed Losses'') and 12 (''Projected Booked Losses'') of FR Y–14M, Schedule D.2 (Portfolio Level Credit Card Information) to require firms to project lifetime losses under current expected credit losses (CECL) projections on a rolling basis each month, as opposed to only losses over the next twelve months on a rolling basis each month. A commenter stated that these proposed revisions do not allow firms to report losses quarterly, which would align with current CECL practices of calculating losses at most firms. A commenter suggested that the Board revise the instructions to provide firms more flexibility for reporting items 11 and 12.

The Board notes that firms should use an appropriate model for calculating projected managed and booked losses that is consistent with current accounting guidelines and firms' own modeling frameworks. Therefore, to allow flexibility in reporting, the Board has removed the language ''rolling basis each reporting month'' from items 11 and 12. Additionally, the Board has not adopted the proposed revisions to the instructions to project through the expected lifetime of the loans for line items 11 and 12. Rather, the Board will continue to require firms to report projected managed and booked losses over the next twelve months for each respective portfolio.

A commenter indicated that the proposed revisions to items 11 and 12 would require firms that have adopted CECL to report duplicative data in these items as they are required to report in Schedule D.2, items 9 (''ALL Managed Balance'') and 10 (''ALL Booked Balance''), respectively. Additionally, the commenter asked the Board to clarify whether the values reported in items 11 and 12 should include projected interest and fees.

Given that the Board has not adopted the revision as proposed to items 11 and 12, the instructions for items 11 and 12 will to continue to differ from those of items 9 and 10. The instructions for items 9 and 10 reflect the lifetime expected credit losses for firms that have adopted CECL, whereas the instructions for items 11 and 12 require institutions that have adopted CECL to report the allowance for credit losses managed or booked balance over the next 12 months, respectively. Also, given the intention to capture total projected losses within items 11 and 12, the Board has clarified the instructions for these items to require firms to include projected losses recognized to on-balance sheet interest and fees.

Legal authorization and confidentiality: The Board has the authority to require BHCs to file the FR Y–14 reports pursuant to section 5(c) of the Bank Holding Company Act (''BHC Act''), 12 U.S.C. 1844(c), and pursuant to section 165(i) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), 12 U.S.C. 5365(i), as amended by section 401(a) and (e) of the Economic Growth, Regulatory Relief, and Consumer Protection Act (EGRRCPA).[11] The Board has authority to require SLHCs to file the FR Y–14 reports pursuant to section 10(b) of the Home Owners' Loan Act (12 U.S.C. 1467a(b)), as amended by section 369(8) and 604(h)(2) of the Dodd-Frank Act. Lastly, the Board has authority to require U.S. IHCs of FBOs to file the FR Y–14 reports pursuant to section 5 of the BHC Act, as well as pursuant to sections 102(a)(1) and 165 of the Dodd-Frank Act, 12 U.S.C. 5311(a)(1) and 5365.[12] In addition, section 401(g) of EGRRCPA, 12 U.S.C. 5365 note, provides that the Board has the authority to establish enhanced prudential standards for foreign banking organizations with total consolidated assets of $100 billion or more, and clarifies that nothing in section 401 ''shall be construed to affect the legal effect of the final rule of the Board . . . entitled 'Enhanced Prudential Standard for [BHCs] and Foreign Banking Organizations' (79 FR 17240 (March 27, 2014)), as applied to foreign banking organizations with total consolidated assets equal to or greater than $100 million.'' [13] The FR Y–14 reports are mandatory. The information collected in the FR Y–14 reports is collected as part of the Board's supervisory process, and therefore, such information is afforded confidential treatment pursuant to exemption 8 of the Freedom of Information Act (FOIA), 5 U.S.C. 552(b)(8). In addition, confidential commercial or financial information, which a submitter actually and customarily treats as private, and which has been provided pursuant to an express assurance of confidentiality by the Board, is considered exempt from disclosure under exemption 4 of the FOIA, 5 U.S.C. 552(b)(4).[14]

Board of Governors of the Federal Reserve System, September 9, 2020.

Michele Taylor Fennell,

Assistant Secretary of the Board.

[FR Doc. 2020–20189 Filed 9–11–20; 8:45 am]

BILLING CODE 6210–01–P

[11] Public Law 115–174, Title IV § 401(a) and (e), 132 Stat. 1296, 1356–59 (2018).

[12] Section 165(b)(2) of the Dodd-Frank Act, 12 U.S.C. 5365(b)(2), refers to ''foreign-based bank holding company.'' Section 102(a)(1) of the Dodd-Frank Act, 12 U.S.C. 5311(a)(1), defines ''bank holding company'' for purposes of Title I of the Dodd-Frank Act to include foreign banking organizations that are treated as bank holding companies under section 8(a) of the International Banking Act of 1978, 12 U.S.C. 3106(a). The Board has required, pursuant to section 165(b)(1)(B)(iv) of the Dodd-Frank Act, 12 U.S.C. 5365(b)(1)(B)(iv), certain foreign banking organizations subject to section 165 of the Dodd-Frank Act to form U.S. intermediate holding companies. Accordingly, the parent foreign-based organization of a U.S. IHC is treated as a BHC for purposes of the BHC Act and section 165 of the Dodd-Frank Act. Because Section 5(c) of the BHC Act authorizes the Board to require reports from subsidiaries of BHCs, section 5(c) provides additional authority to require U.S. IHCs to report the information contained in the FR Y–14 reports.

[13] The Board's Final Rule referenced in section 401(g) of EGRRCPA specifically stated that the Board would require IHCs to file the FR Y–14 reports. *See* 79 FR 17240, 17304 (March 27, 2014).

[14] Please note that the Board publishes a summary of the results of the Board's CCAR testing pursuant to 12 CFR 225.8(f)(2)(v), and publishes a summary of the results of the Board's DFAST stress testing pursuant to 12 CFR 252.46(b) and 12 CFR 238.134, which includes aggregate data. In addition, under the Board's regulations, covered companies must also publicly disclose a summary of the results of the Board's DFAST stress testing. *See* 12 CFR 252.58; 12 CFR 238.146. The public disclosure requirement contained in 12 CFR 252.58 for covered BHCs and covered IHCs is separately accounted for by the Board in the Paperwork Reduction Act clearance for FR YY (OMB No. 7100–0350) and the public disclosure requirement for covered SLHCs is separately accounted for in by the Board in the Paperwork Reduction Act clearance for FR LL (OMB No. 7100–0380).

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 applications are set forth in paragraph 7 of the Act (12 U.S.C. 1817(j)(7)).

The public portions of 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(s) indicated below and at the offices of the Board of Governors. This information may also be obtained on an expedited basis, upon request, by contacting the appropriate Federal Reserve Bank and from the Board's Freedom of Information Office at *https://www.federalreserve.gov/foia/request.htm.* 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 Street and Constitution Avenue NW, Washington, DC 20551–0001, not later than September 29, 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. *The SSX3 Trust, The SSX4 Trust, and William G. Smith, III, as trustee of both trusts, all of Tallahassee, Florida;* to join the Smith Family Control Group, a group acting in concert, and retain voting shares of Capital City Bank Group, Inc., and thereby indirectly retain voting shares of Capital City Bank, both of Tallahassee, Florida.

Board of Governors of the Federal Reserve System, September 9, 2020.

Yao-Chin Chao,

Assistant Secretary of the Board.

[FR Doc. 2020–20203 Filed 9–11–20; 8:45 am]

BILLING CODE 6210–01–P

GENERAL SERVICES ADMINISTRATION

[Notice MA–2020–07; Docket No. 2020–0002, Sequence No. 20]

Request for Public Comment: Methodologies To Identify Excess Personal Property

AGENCY: General Services Administration (GSA).

ACTION: Notice.

SUMMARY: GSA is seeking input on methodologies to identify personal property as excess. See the **SUPPLEMENTARY INFORMATION** section below for additional guidance.

DATES: Comments must be received on or before November 13, 2020.

ADDRESSES: Submit comments identified by ''Notice–MA–2020–07, Methodologies to Identify Excess Personal Property'' by any of the following methods:

- *Regulations.gov: http://www.regulations.gov.* Submit comments via the Federal eRulemaking portal by searching for Notice–MA–2020–07, Methodologies to Identify Excess Personal Property. Select the link ''Comment Now'' that corresponds with ''Notice MA–2020–07, Methodologies to Identify Excess Personal Property.'' Follow the instructions provided on the screen. Please include your name, company name (if applicable), and ''Notice–MA–2020–07, Methodologies to Identify Excess Personal Property'' on your attached document.

FOR FURTHER INFORMATION CONTACT: Mr. William Garrett, Director, Personal Property, Office of Government-wide Policy, 202–368–8163 or via email at *william.garrett@gsa.gov.*

SUPPLEMENTARY INFORMATION: In January 2018, the Federal Personal Property Management Act (FPPMA), Public Law 115–419, was enacted requiring agencies to regularly assess certain types of personal property under their control in accordance with guidance from GSA. Subsequently, on December 20, 2019, GAO published its final report GAO–20–228, ''Federal Property: GSA Guidance Needed to Help Agencies Identify Unneeded Property in Warehouses.'' The report concluded, in part, ''with the recent enactment of FPPMA, an opportunity exists for GSA to develop and communicate guidance to help agencies assess property utilization and identify unneeded property in warehouses more efficiently that includes practices GSA identifies as being useful.'' The report concluded that the Administrator of General Services should ''direct the Office of Government-wide Policy (1) to incorporate into its guidance approaches or practices that agencies could use to assess utilization of and the ongoing need for property—approaches such as recommendations for periodic justifications, data analytics, and utilization reviews—and (2) to develop a plan and timelines for communicating the guidance to agencies government-wide.'' To address these recommendations, in part, GSA established a working group of Federal and industry personal property management experts. GSA is soliciting input from the public to inform GSA and the working group of existing methodologies to effectively identify excess personal property.

Although GSA may not respond to each individual comment, GSA may follow-up with respondents to clarify input. GSA values public feedback and will consider all comments that it receives. GSA will also be conducting targeted outreach on this same topic, including engaging with subject matter experts to improve internal guidance.

Jessica Salmoiraghi,

Associate Administrator, Office of the Administrator.

[FR Doc. 2020–18209 Filed 9–11–20; 8:45 am]

BILLING CODE 6820–14–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

Healthcare Infection Control Practices Advisory Committee

AGENCY: Centers for Disease Control and Prevention (CDC), Department of Health and Human Services (HHS).

ACTION: Notice of meeting.

SUMMARY: In accordance with the Federal Advisory Committee Act, the CDC announces the following meeting for the Healthcare Infection Control Practices Advisory Committee (HICPAC). This meeting is open to the public, limited only by audio phone lines available. The public is also welcome to listen to the meeting by dialing 1–877–924–1748, passcode: 6118574. A total of 200 lines will be available. Registration is required. To register for this call, please go to *www.cdc.gov/hicpac.*

DATES: The meeting will be held on November 5, 2020, from 9:00 a.m. to 3:00 p.m., EST.

ADDRESSES: The teleconference access is 1–877–924–1748, and the passcode is 6118574.

FOR FURTHER INFORMATION CONTACT: Koo-Whang Chung, M.P.H., HICPAC, Division of Healthcare Quality Promotion, NCEZID, CDC, l600 Clifton Road, NE, Mailstop H16–3, Atlanta, Georgia 30329–4027, Telephone (404) 498–0730; Email: *HICPAC@cdc.gov.*

SUPPLEMENTARY INFORMATION:

Purpose: The Committee is charged with providing advice and guidance to the Director, Division of Healthcare Quality Promotion (DHQP), the Director, National Center for Emerging and Zoonotic Infectious Diseases (NCEZID), the Director, CDC, the Secretary, Health and Human Services regarding 1) the practice of healthcare infection prevention and control; 2) strategies for surveillance, prevention, and control of infections, antimicrobial resistance, and related events in settings where healthcare is provided; and 3) periodic updating of CDC guidelines and other policy statements regarding prevention of healthcare-associated infections and healthcare-related conditions.

Matters To Be Considered: The agenda will include updates from the following HICPAC workgroups: The Healthcare Personnel Guideline Workgroup; the Long-term Care/Post-acute Care Workgroup; and the Neonatal Intensive Care Unit Workgroup. Agenda items are subject to change as priorities dictate.

Procedure for Public Comment: Time will be available for public comment. Members of the public who wish to provide public comments should plan to attend the public comment session at the start time listed. Please note that the public comment period may end before the time indicated, following the last call for comments.

Procedure for Public Written Comment: The public may submit written comments in advance of the meeting. Comments should be submitted in writing by email to the contact person listed above. The deadline for receipt of written public comment is October 21, 2020. All requests must contain the name, address, and organizational affiliation of the speaker, as well as the topic being addressed. Written comments should not exceed one single-spaced typed page in length. Written comments received in advance of the meeting will be included in the official record of the meeting.

The Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention, has been delegated the authority to sign **Federal Register** notices pertaining to announcements of meetings and other committee management activities, for both the Centers for Disease Control and Prevention and the Agency for Toxic Substances and Disease Registry.

Kalwant Smagh,

Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention.

[FR Doc. 2020–20183 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

Healthcare Infection Control Practices Advisory Committee; Notice of Charter Amendment

AGENCY: Centers for Disease Control and Prevention (CDC), Department of Health and Human Services (HHS).

ACTION: Notice of charter amendment.

SUMMARY: This gives notice under (the Federal Advisory Committee Act of October 6, 1972, that the Healthcare Infection Control Practices Advisory Committee (HICPAC), Centers for Disease Control and Prevention, Department of Health and Human Services, has amended their charter in the Description of Duties and Agency or Official to whom the Committee reports, and sections throughout the document as follows: (1) The Office of Infectious Diseases (OID) has been renamed the Deputy Director for Infectious Diseases (DDID); (2) the Healthcare Facilities Accreditation Program and the National Association of Directors of Nursing Administration as non-voting liaison representatives have been removed; and (3) the addition of non-voting liaisons from the Organization for Safety, Asepsis, and Prevention; the National Rural Health Association; and the Patient Safety Action Network; and the addition of a non-voting ex officio member from the Indian Health Service. The amended filing date is August 28, 2020.

FOR FURTHER INFORMATION CONTACT: Michael Bell, M.D., Designated Federal Officer, HICPAC, Division of Healthcare Quality Promotion, National Center for Emerging and Zoonotic Infectious Diseases, CDC, l600 Clifton Road, NE, MS H16–3, Atlanta, Georgia 30329–4027; Telephone: 404–639–4000; Email: *hicpac@cdc.gov.*

The Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention, has been delegated the authority to sign **Federal Register** notices pertaining to announcements of meetings and other committee management activities, for both the Centers for Disease Control and Prevention and the Agency for Toxic Substances and Disease Registry.

Kalwant Smagh,

Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention.

[FR Doc. 2020–20184 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

[60Day–20–1227; Docket No. CDC–2020–0097]

Proposed Data Collection Submitted for Public Comment and Recommendations

AGENCY: Centers for Disease Control and Prevention (CDC), Department of Health and Human Services (HHS).

ACTION: Notice with comment period.

SUMMARY: The Centers for Disease Control and Prevention (CDC), as part of its continuing effort to reduce public burden and maximize the utility of government information, invites the general public and other Federal agencies the opportunity to comment on a proposed and/or continuing information collection, as required by the Paperwork Reduction Act of 1995. This notice invites comment on a proposed revision to an information collection project titled ''Assessment of Ill Worker Policies Study.'' The study will examine whether an educational intervention has an effect on restaurants either developing or expanding their ill worker management policies.

DATES: CDC must receive written comments on or before November 13, 2020.

ADDRESSES: You may submit comments, identified by Docket No. CDC–2020–0097 by any of the following methods:

- *Federal eRulemaking Portal: Regulations.gov*. Follow the instructions for submitting comments.
- *Mail:* Jeffrey M. Zirger, Information Collection Review Office, Centers for Disease Control and Prevention, 1600 Clifton Road NE, MS–D74, Atlanta, Georgia 30329.

Instructions: All submissions received must include the agency name and Docket Number. CDC will post, without change, all relevant comments to *Regulations.gov.*

Please note: *Submit all comments through the Federal eRulemaking portal (regulations.gov) or by U.S. mail to the address listed above.*

FOR FURTHER INFORMATION CONTACT: To request more information on the proposed project or to obtain a copy of the information collection plan and instruments, contact Jeffrey M. Zirger, Information Collection Review Office, Centers for Disease Control and Prevention, 1600 Clifton Road NE, MS–D74, Atlanta, Georgia 30329; phone: 404–639–7118; Email: *omb@cdc.gov.*

SUPPLEMENTARY INFORMATION: Under the Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3501–3520), Federal agencies must obtain approval from the Office of Management and Budget (OMB) for each collection of information they conduct or sponsor. In addition, the PRA also requires Federal agencies to provide a 60-day notice in the **Federal Register** concerning each proposed collection of information, including each new proposed collection, each proposed extension of existing collection of information, and each reinstatement of previously approved information collection before submitting the collection to the OMB for approval. To comply with this requirement, we are publishing this notice of a proposed data collection as described below.

The OMB is particularly interested in comments that will help:

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 submissions of responses.
5. Assess information collection costs.

Proposed Project

Assessment of Ill Worker Policies Study (OMB Control No. 0920–1227, Exp. 05/31/2021)—Revision—National Center for Environmental Health

(NCEH), Centers for Disease Control and Prevention (CDC).

Background and Brief Description

The CDC is requesting a three-year Paperwork Reduction Act (PRA) clearance for a Revision to an information collection request (ICR) for a research program focused on identifying the environmental causes of foodborne illness and improving environmental public health practice. This research program is conducted by the Environmental Health Specialists Network (EHS-Net), a collaborative project of the CDC, U.S. Food and Drug Administration (FDA), U.S. Department of Agriculture (USDA), and eight state and local public health programs (California; Tennessee; Minnesota; Rhode Island; New York; New York City, NY; Southern Nevada Health District, NV; and Harris County, TX).

This ICR aims to assess whether an educational intervention will result in either the development or enhancement of restaurant ill worker policies. This will be accomplished by interviewing restaurant managers, surveying workers, and observing restaurant practices in 320 randomly selected and assigned restaurants in the EHS-Net catchment area. Burden hours would be associated with the restaurant staff for the time to answer questions about their restaurant. There would be two to three site visits depending upon which group the restaurants were assigned to, that is, the intervention or the control group. An initial visit will be used to observe baseline conditions and to provide the intervention only to the restaurants selected to receive it. A second visit will be used to determine if the policies had changed and to introduce the intervention to the control restaurants (if it is deemed successful), and a final follow up visit to the control restaurants that received the intervention on the second visit.

Although approved in 2018, NCEH and its program partners needed to prioritize other data collections over this study, and then had to delay the current study due to the COVID–19 pandemic. NCEH partners provided feedback to refine this research protocol, revise the ICR, and plan to begin this study in 2021. NCEH is requesting approval for revisions which fall into three categories: (1) Changes to comply with the 2018 Revised Common Rule and 21st Century Cures Act; (2) changes to strengthen the study, based on recent experience and stakeholder feedback; and (3) changes to respond to the COVID–19 pandemic.

NCEH is requesting a revised PRA clearance for 715 responses per year and for a time burden of 206 hours per year. These changes result in a decrease of 1,412 responses and 146 hours per year relative to the 2018 PRA clearance. There is no cost to the respondents other than their time.

ESTIMATED ANNUALIZED BURDEN HOURS

Type of respondent	Form name	Number of respondents	Number of responses per respondent	Average burden per response (in hr)	Total burden (in hr)
Restaurant Managers (Intervention Restaurants).	Manager Recruiting Script	119	1	3/60	6
Manager Informed Consent and Interview Form.	53	2	20/60	35	
Restaurant Managers (Control Restaurants).	Manager Recruiting Script	119	1	3/60	6
Manager Informed Consent and Interview Form.	53	3	20/60	53	
Health Department Workers (Intervention Restaurants).	Restaurant Environment Observation Form.	53	2	30/60	53
Health Department Workers (Control Restaurants).	Restaurant Environment Observation Form.	53	2	30/60	53
Total					206

Jeffrey M. Zirger,

Lead, Information Collection Review Office, Office of Scientific Integrity, Office of Science, Centers for Disease Control and Prevention.

[FR Doc. 2020–20215 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

[60Day–20–1080; Docket No. CDC–2020–0098]

Proposed Data Collection Submitted for Public Comment and Recommendations

AGENCY: Centers for Disease Control and Prevention (CDC), Department of Health and Human Services (HHS).

ACTION: Notice with comment period.

SUMMARY: The Centers for Disease Control and Prevention (CDC), as part of its continuing effort to reduce public burden and maximize the utility of government information, invites the general public and other Federal agencies the opportunity to comment on a proposed and/or continuing information collection, as required by the Paperwork Reduction Act of 1995. This notice invites comment on a proposed information collection project titled HIV Outpatient Study (HOPS). The Centers for Disease Control and Prevention is requesting a three-year extension to the previously approved project to continue collecting standardized HIV clinical and behavioral data at private HIV care practices and university based U.S. clinics participating in the HOPS.

DATES: CDC must receive written comments on or before November 13, 2020.

ADDRESSES: You may submit comments, identified by Docket No. CDC–2020–0098 by any of the following methods:

- *Federal eRulemaking Portal: Regulations.gov*. Follow the instructions for submitting comments.
- *Mail:* Jeffrey M. Zirger, Information Collection Review Office, Centers for Disease Control and Prevention, 1600 Clifton Road NE, MS–D74, Atlanta, Georgia 30329.

Instructions: All submissions received must include the agency name and Docket Number. CDC will post, without change, all relevant comments to *Regulations.gov*.

Please note: *Submit all comments through the Federal eRulemaking portal (*regulations.gov*) or by U.S. mail to the address listed above.*

FOR FURTHER INFORMATION CONTACT: To request more information on the proposed project or to obtain a copy of the information collection plan and instruments, contact Jeffrey M. Zirger, Information Collection Review Office, Centers for Disease Control and Prevention, 1600 Clifton Road NE, MS–D74, Atlanta, Georgia 30329; phone: 404–639–7118; Email: *omb@cdc.gov.*

SUPPLEMENTARY INFORMATION: Under the Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3501–3520), Federal agencies must obtain approval from the Office of Management and Budget (OMB) for each collection of information they conduct or sponsor. In addition, the PRA also requires Federal agencies to provide a 60-day notice in the **Federal Register** concerning each proposed collection of information, including each new proposed collection, each proposed extension of existing collection of information, and each reinstatement of previously approved information collection before submitting the collection to the OMB for approval. To comply with this requirement, we are publishing this notice of a proposed data collection as described below.

The OMB is particularly interested in comments that will help:

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 submissions of responses.

5. Assess information collection costs.

Proposed Project

HIV Outpatient Study (HOPS) (OMB Control No. 0920–1080, Exp. 09/30/2021)—Extension—National Center for HIV/AIDS, Viral Hepatitis, STD, and TB Prevention (NCHHSTP), Centers for Disease Control and Prevention (CDC).

Background and Brief Description

The Centers for Disease Control and Prevention requests a three-year approval for the HIV Outpatient Study data collection activity. The HIV Outpatient Study (HOPS) is a prospective longitudinal cohort of HIV-infected outpatients at eight well established private HIV care practices and university-based U.S. clinics, in Tampa, Florida; Washington, DC; Stony Brook, New York; Chicago, Illinois; Denver, Colorado; and Philadelphia, Pennsylvania. Clinical data are abstracted on an ongoing basis from the medical records of adult HIV-infected HOPS study participants, who also complete an optional telephone/Web-based behavioral assessment as part of their annual clinic visit, which on average takes about seven minutes. Before enrolling in this study, all potential study participants will undergo an informed consent process (including signing of a written informed consent) which is estimated to take 15 minutes.

The core areas of HOPS research extending through the present HIV treatment era include; (i) monitoring death rates and causes of death, (ii) characterizing the optimal patient management strategies to reduce HIV related morbidity and mortality (*e.g.,* effectiveness of antiretroviral therapies and other clinical interventions), (iii) monitoring of sexual and drug use behaviors to inform Prevention with Positives, and (iv) investigating disparities in the HIV care continuum by various demographic factors.

In recent years, the HOPS has been instrumental in bringing attention to emerging issues in chronic HIV infection with actionable opportunities for prevention, including cardiovascular disease, fragility fractures, renal and hepatic disease, and cancers. The HOPS remains an important source for multiyear trend data concerning conditions and behaviors for which data are not readily available elsewhere, including: rates of opportunistic illnesses, rates of comorbid conditions (*e.g.,* hypertension, obesity, diabetes) and antiretroviral drug resistance.

Data will be collected through medical record abstraction by trained abstractors and by telephone or internet based, computer-assisted interviews at eight funded study sites in six U.S. cities. Collection of data abstracted from patient medical records provides data in five general categories: Demographics and risk behaviors for HIV infection; symptoms; diagnosed conditions (definitive and presumptive); medications prescribed (including dose, duration, and reasons for stopping); all laboratory values, including CD4+ T-lymphocyte (CD4+) cell counts, plasma HIV–RNA determinations, and genotype, phenotype, and trophile results. Data on visit frequency, AIDS, and death are acquired from the clinic chart. Data collected using a brief Telephone Audio-Computer Assisted Self-Interview (T–ACASI) survey or an identical Web-based Audio-Computer Assisted Self-Interview (ACASI) include: Age, sex at birth, use of alcohol and drugs, cigarette smoking, adherence to antiretroviral medications, types of sexual intercourse, condom use, and disclosure of HIV status to partners.

We anticipate that 450 new HOPS study participants will be recruited annually into the HOPS from a pool of HIV-infected individuals currently in HIV-care at the nine aforementioned clinics (50 patients per site). Patients are approached during one of their routine clinic visits to participate in the HOPS. Patients interested in participating in the HOPS are given detailed information about the nature of the study and provided with written informed consent that must be completed prior to enrollment. The 450 newly enrolled participants each year will be added to the database of existing participants such that approximately 2,500 participants will be seen in the HOPS each year. Medical record abstractions will be completed on all HOPS participants and impose no direct burden on HOPS study participants. Participation of respondents is voluntary. There is no cost to the respondents other than their time.

ESTIMATED ANNUALIZED BURDEN HOURS

Type of respondent	Form name	Number of respondents	Number of responses per respondent	Average burden per response (in hr)	Total burden (in hr)
HOPS study Patients	Behavioral survey	2,500	1	7/60	292
HOPS Study Patients	Consent form	450	1	15/60	113
Total		405			

Jeffrey M. Zirger,

Lead, Information Collection Review Office, Office of Scientific Integrity, Office of Science, Centers for Disease Control and Prevention.

[FR Doc. 2020–20214 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

Board of Scientific Counselors, Center for Preparedness and Response

AGENCY: Centers for Disease Control and Prevention (CDC), Department of Health and Human Services (HHS).

ACTION: Notice of meeting.

SUMMARY: In accordance with the Federal Advisory Committee Act, the CDC announces the following meeting for the Board of Scientific Counselors, Center for Preparedness and Response, (BSC, CPR). This is a virtual meeting that is open to the public, limited only by the number of net conference access available, which is 500. Pre-registration is required by accessing the link at *https://cdc.zoomgov.com/webinar/register/WN_bV_Jrvp4QZGHZFao0moqPg.*

DATES: The meeting will be held on October 26, 2020, from 12:30 p.m. to 3:30 p.m., EDT.

ADDRESSES: Zoom Virtual Meeting. If you wish to attend the virtual meeting, please pre-register by accessing the link at *https://cdc.zoomgov.com/webinar/register/WN_bV_Jrvp4QZGHZFao0moqPg.*

Instructions to access the Zoom virtual meeting will be provided in the link following registration.

FOR FURTHER INFORMATION CONTACT: Dometa Ouisley, Office of Science and Public Health Practice, Centers for Disease Control and Prevention, 1600 Clifton Road NE, Mailstop-H21–6, Atlanta, Georgia 30329–4027, Telephone: (404) 639–7450; Facsimile: (404) 471–8772; Email: *OPHPR.BSC.Questions@cdc.gov.*

SUPPLEMENTARY INFORMATION:

Purpose: This Board is charged with providing advice and guidance to the Secretary, Department of Health and Human Services (HHS), the Assistant Secretary for Health (ASH), the Director, Centers for Disease Control and Prevention (CDC), and the Director, Center for Preparedness and Response (CPR), concerning strategies and goals for the programs and research within CPR, monitoring the overall strategic direction and focus of the CPR Divisions and Offices, and administration and oversight of peer review for CPR scientific programs. For additional information about the Board, please visit: *https://www.cdc.gov/cpr/bsc/index.htm.*

Matters To Be Considered: The agenda will include discussions on updates from the CPR Director and Division Directors, CPR Strategic Planning and Science Agenda, and CPR BSC Polio Containment Workgroup (PCWG) Updates. Agenda items are subject to change as priorities dictate.

The Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention, has been delegated the authority to sign **Federal Register** notices pertaining to announcements of meetings and other committee management activities, for both the Centers for Disease Control and Prevention and the Agency for Toxic Substances and Disease Registry.

Kalwant Smagh,

Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention.

[FR Doc. 2020–20187 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

A National Elastomeric Half Mask Respirator (EHMR) Strategy for Use in Healthcare Settings During an Infectious Disease Outbreak/Pandemic

AGENCY: National Institute for Occupational Safety and Health (NIOSH) of the Centers for Disease Control and Prevention (CDC), Department of Health and Human Services (HHS).

ACTION: Request for information and comment.

SUMMARY: The National Institute for Occupational Safety and Health (NIOSH) of the Centers for Disease Control and Prevention (CDC), within the Department of Health and Human Services (HHS), announces this request for information regarding the deployment and use of elastomeric half-mask respirators in healthcare settings and emergency medical services (EMS) organizations during the COVID–19 crisis.

DATES: Comments must be received October 14, 2020.

ADDRESSES: Responses should be submitted to Dr. Lee Greenawald, NIOSH, 626 Cochrans Mill Road, Building 141, Pittsburgh, PA 15236, or *ppeconcerns@cdc.gov.*

FOR FURTHER INFORMATION CONTACT: Lee Greenawald, NIOSH, 626 Cochrans Mill Road, Building 141, Pittsburgh, PA 15236; phone: (412) 386–6465 (not a toll-free number, email: *ppeconcerns@cdc.gov.*

SUPPLEMENTARY INFORMATION:

Public Participation

Informational submissions in response to this request for information (RFI) are due no later than October 14, 2020. Please limit informational submissions for each of the two sections to five pages or less (for a total of 10 pages or less).

NIOSH will not respond to individual informational submissions or publish publicly a compendium of responses. An informational submission in response to this RFI does not create any commitment on or behalf of CDC or HHS to develop or pursue the program or ideas discussed.

Respondents are requested to provide the following information at the start of their informational submission in response to this RFI:

- Company/institution name;
- Company/institution contact;
- Contact's address, phone number, and email address.

Please provide any additional relevant background information about yourself or your organization but note that submissions will not be redacted.

Introduction

An elastomeric half-mask respirator (EHMR) is a non-powered air-purifying respirator that has a tight-fitting facepiece that covers the nose and mouth. The facepieces are made of synthetic or natural rubber material permitting repeated cleaning, disinfection, storage, and reuse. EHMRs use replaceable filters or cartridges, and they provide at least the same level of protection as single-use N95 filtering facepiece respirators (FFRs). As outlined in the Code of Federal Regulations,[1] all EHMR models used in U.S. workplaces must be evaluated and approved by NIOSH's National Personal Protective Technology Laboratory (NPPTL). In 2018, NIOSH/NPPTL sponsored a National Academies of Sciences, Engineering, and Medicine Consensus Study Report [2] that discussed the feasibility of reusable respirator use (including EHMRs) for routine and surge situations in U.S. healthcare organizations. The National Academies' report also recommended various EHMR-related research activities related to cleaning/disinfection, fit testing, cost/market analyses for EHMRs introduced to healthcare, and healthcare user acceptability considerations.

Although EHMRs have been used routinely in healthcare settings, they are not considered medical devices pursuant to the Federal Food, Drug, and Cosmetic Act (FD&C Act) and thus are not typically authorized for use as U.S. Food and Drug Administration (FDA)-approved medical devices. However, in response to the COVID–19 crisis, FDA has issued an emergency use authorization (EUA) authorizing the ''emergency use of medical devices, including alternative products used as medical devices, pursuant to section 564 of the FD&C Act,'' including EHMRs.[3] The Strategic National Stockpile (SNS) plans to purchase EHMRs to be deployed to and used by healthcare organizations in order to diversify the respiratory protection options available to healthcare workers and emergency responders during the COVID–19 crisis.

NIOSH anticipates that the widespread use of EHMRs will ease the demand for single-use N95 FFRs in healthcare settings experiencing high numbers of COVID–19 patients. In media reports about the COVID–19 crisis, medical professionals have noted that the use of EHMRs has been critical to the response, especially during shortages of N95 FFRs. Wearers note that EHMRs are comfortable to wear, and that given their low cost, ease of use, and ability to be cleaned and decontaminated, hospitals have found these devices to be valuable in keeping workers safe.[4]

In order to gather more information from EHMR users in healthcare and emergency response settings, NIOSH is seeking input on two related endeavors: A deployment of EHMRs across the nation from the SNS, and future NIOSH EHMR demonstration projects. NIOSH's specific information needs are described below.

Defining a National Strategy To Inform the Purchase, Deployment, and Use of Reusable EHMRs in Healthcare Settings During an Infectious Disease Outbreak/Pandemic

NIOSH seeks information and ideas that may be used by the SNS to conduct a program to solicit and obtain a diverse group of healthcare organizations to participate in a deployment of EHMRs across the nation.

The intent is for the SNS to provide participating organizations with a fixed quantity of the EHMR devices it purchases to use in their healthcare activities. Each participating organization will also receive the EHMR Best Practice Guidelines/Hospital Implementation Guide prepared by NIOSH. Each participating organization will provide NIOSH a detailed report of its experiences using the EHMRs, including user acceptability and feasibility of implementation. These reports will inform future updates to the Best Practice Guidelines/Hospital implementation Guide.

The types of potential participant organizations that will be sought include, but are not limited to, hospital systems, hospitals, hospital intensive care units (ICUs), hospital general wards, hospital emergency departments, outpatient care settings, nursing homes, dental organizations, and first responders, including, but not limited to, emergency medical services, police officers, and firefighters.

Please provide responses to one or both of the following:

1. Provide a Statement of Interest (SOI) to participate in the deployment of EHMRs across the nation:

a. Describe the nature of the organization that desires to participate, including type, geographical location (including rural or urban), size (*e.g.,* hospital beds, healthcare staff), and prior experience with the organizational use of EHMRs. Although prior experience with EHMRs is not required, any EHMR experience can be specified, including manufacturers, model numbers, and quantity of devices used;

b. Describe the proposed approach regarding how the received EHMRs would be implemented into the organization (*e.g.,* strategy for distribution to the appropriate staff and care settings); and

c. Describe the interested participant's commitment to developing a report based on the EHMR experiences of staff.

2. Provide information that will assist the SNS and NIOSH in the following:

a. Defining the strategic parameters of this distribution program; for example, considerations about fit testing, training, education, filter change-out schedule, cleaning/disinfection, storage considerations, and appropriate clinical care settings for EHMR use; and

b. The potential criteria to be used to determine how the purchased devices should be distributed; for example, the technical approach of the use of the EHMRs, and technical qualifications of key staff who would lead the initiative.

Interest in Participating and Refining Additional, Future, EHMR Demonstration Projects

In addition to NIOSH's current EHMR research activities, NIOSH is considering conducting additional EHMR demonstration projects. These EHMR demonstration projects would consist of healthcare or EMS organizations using EHMRs in their respiratory protection programs and providing user acceptability feedback, such as on fit testing and disinfection protocols, among other implementation parameters. The full scope of these additional EHMR demonstration projects is still being defined. NIOSH

[1] 42 CFR part 84—Approval of Respiratory Protective Devices. *https://ecfr.io/Title-42/Part-84.*

[2] *https://www.nap.edu/catalog/25275/reusable-elastomeric-respirators-in-health-care-considerations-for-routine-and.*

[3] 85 FR 17335 (March 27, 2020).

[4] Hamby C. May 2020. They Evoke Darth Vader, but These Masks May Save your Doctor's Life. *https://www.nytimes.com/2020/05/27/us/coronavirus-masks-elastomeric-respirators.html.*

seeks information on interest in participating as a future demonstration site to gauge interest in the nationwide implementation of using EHMRs in hospital and EMS settings to supplement current respiratory protection program activities, and to collect additional user input parameters not currently being collected in the current activities.

The types of potential participant organizations that will be sought include, but are not limited to, hospital systems, hospitals, hospital intensive care units (ICUs), hospital general wards, hospital emergency departments, outpatient care settings, nursing homes, dental organizations, and first responders, including, but not limited to, EMS, police officers, and firefighters.

Please provide responses to one or both of the following:

1. Provide a Statement of Interest (SOI) describing interest in participating in future EHMR demonstration project activities. The SOI should describe the nature of the organization that desires to participate as a demonstration site, including type, geographical location (including rural or urban), size (*e.g.,* hospital beds, healthcare staff), and prior organizational experience with the use of EHMRs. The SOI should also provide reasons for interest in participating as a demonstration site. Prior experience with the use of EHMRs will NOT be required to participate in the EHMR demonstration project activity. The description of an approach that has the potential to be effective for conducting a demonstration project will be required.

2. Provide information that will assist NIOSH in the refinement of the EHMR demonstration projects, including the following:

a. Defining the strategic parameters of this EHMR demonstration activity; for example, considerations of fit testing, training, education, filter change-out schedule, cleaning/disinfection, storage considerations, and appropriate clinical care settings for EHMR use; and

b. The potential criteria to be used to determine how the EHMR devices should be distributed to the demonstration sites; for example, the technical approach of the use of the EHMRs, and technical qualifications of key staff who would lead the initiative.

No SNS Applications Will Be Accepted Through This RFI

While the strategy for distribution of the purchased EHMRs is being developed, its details will only be finalized after consideration and analysis of the informational submissions in response to this RFI.

Disclaimer and Important Notes

This RFI is for planning purposes; it does not constitute a formal announcement for comprehensive applications. In accordance with Federal Acquisition Regulation 48 CFR 15.201(e), responses to this RFI are not offers and cannot be accepted by the Government to form a binding award. NIOSH will not provide reimbursement for costs incurred in responding to this RFI.

Dated: September 8, 2020.

John J. Howard,

Director, National Institute for Occupational Safety and Health, Centers for Disease Control and Prevention, Department of Health and Human Services.

[FR Doc. 2020–20115 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

[30Day–20–0106]

Agency Forms Undergoing Paperwork Reduction Act Review

In accordance with the Paperwork Reduction Act of 1995, the Centers for Disease Control and Prevention (CDC) has submitted the information collection request titled Preventive Health and Health Services Block Grant to the Office of Management and Budget (OMB) for review and approval. CDC previously published a ''Proposed Data Collection Submitted for Public Comment and Recommendations'' notice on 05/21/2020 to obtain comments from the public and affected agencies. CDC received one comment related to the previous notice. This notice serves to allow an additional 30 days for public and affected agency comments.

CDC will accept all comments for this proposed information collection project. The Office of Management and Budget is particularly interested in comments that:

(a) 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;

(b) Evaluate the accuracy of the agencies estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used;

(c) Enhance the quality, utility, and clarity of the information to be collected;

(d) 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; and

(e) Assess information collection costs.

To request additional information on the proposed project or to obtain a copy of the information collection plan and instruments, call (404) 639–7570. Comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *www.reginfo.gov/public/do/PRAMain* Find this particular information collection by selecting ''Currently under 30-day Review—Open for Public Comments'' or by using the search function. Direct written comments and/or suggestions regarding the items contained in this notice to the Attention: CDC Desk Officer, Office of Management and Budget, 725 17th Street NW, Washington, DC 20503 or by fax to (202) 395–5806. Provide written comments within 30 days of notice publication.

Proposed Project

Preventive Health and Health Services Block Grant (OMB Control No. 0920–0106, Exp.08/31/2022)—Revision—Center for State, Tribal, Local, and Territorial Support (CSTLTS), Centers for Disease Control and Prevention (CDC).

Background and Brief Description

CDC's Center for State, Tribal, Local, and Territorial Support (CSTLTS) plays a vital role in helping health agencies work to enhance their capacity and improve their performance to strengthen the public health system on all levels. CSTLTS is CDC's primary connection to health officials and leaders of state, tribal, local, and territorial public health agencies, as well as to other government leaders who work with health departments.

CSTLTS administers the Preventive Health and Health Services (PHHS) Block Grant funding for health promotion and disease prevention programs. Sixty-one recipients (50 states, the District of Columbia, two American Indian tribes, five U.S. territories, and three freely associated states) receive block grant funds to address locally defined public health needs in innovative ways. The PHHS Block Grant allows recipients to prioritize the use of funds to fill funding gaps in programs that deal with leading causes of death and disability, as well as the ability to respond rapidly to emerging health issues, including outbreaks of food-borne infections and water-borne diseases. CSTLTS ensures that the CDC PHHS Block Grant Program Manager and recipients account for funds in accordance with legislative mandates. Each recipient is required to submit a work plan with its selected health outcome objectives, as well as descriptions of the health problems, identified target populations (including portions of those populations disproportionately affected by the health problems), and activities to be addressed in the planned work. CDC will use the Block Grant Information System to collect recipient data, monitor recipients' progress, identify activities and personnel supported with Block Grant funding, conduct compliance reviews of Block Grant recipients, and promote the use of evidence-based guidelines and interventions.

CDC requests OMB approval for revision of this existing information collection request to accommodate the needed updates to the system and templates used to collect the information. As specified in the authorizing legislation, CDC currently collects information from Block Grant recipients to monitor their objectives and activities. Recipients will submit information on the following:

• *Recipient information:* Unique identifying information about each recipient.
• *Work plan:* Information about objectives, activities, and the populations to be addressed each year.
• *Annual Progress Report:* Information about success and progress toward meeting health objectives.

Since 2008, CDC has collected this information using a web-based electronic system, the Block Grant Management Information System (BGMIS). Beginning with the FY2021 award, CDC will begin using a new information management system, the Block Grant Information System (BGIS) to collect this information. The new system will essentially collect the same information as the old system, but will offer a variety of updates and improvements. Examples of improvements include updated technological infrastructure, updated Healthy People Objectives (from 2020 to 2030) for recipients to use when planning programs, usability improvements, and redesigned instruments to capture data in more useful formats for both the recipients and reporting purposes.

The respondent universe will include PHHS Block Grant Coordinators(n=61). All modules will be accessed electronically through the BGIS system. CDC requests approval for an estimated 1,525 burden hours annually.

ESTIMATED ANNUALIZED BURDEN HOURS

Type of respondents	Form name	Number of respondents	Number of responses per respondent	Average burden per response (in hours)
PHHS Block Grant Coordinator	Recipient Information	61	1	2
PHHS Block Grant Coordinator	Work Plan	61	1	12
PHHS Block Grant Coordinator	PHHS Block Annual Progress Report	61	1	11

Jeffrey M. Zirger,
Lead, Information Collection Review Office, Office of Scientific Integrity, Office of Science, Centers for Disease Control and Prevention.

[FR Doc. 2020–20213 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Centers for Disease Control and Prevention

Clinical Laboratory Improvement Advisory Committee (CLIAC)

AGENCY: Centers for Disease Control and Prevention (CDC), Department of Health and Human Services (HHS).

ACTION: Notice of meeting.

SUMMARY: In accordance with the Federal Advisory Committee Act, the CDC announces the following meeting for the Clinical Laboratory Improvement Advisory Committee (CLIAC). This meeting is open to the public, limited only by the webcast lines available. Check the CLIAC website on the day of the meeting for the web conference link *www.cdc.gov/cliac.*

DATES: The meeting will be held on October 28, 2020, from 11:00 a.m. to 6:30 p.m., EDT and October 29, 2020, from 11:00 a.m. to 3:00 p.m., EDT.

ADDRESSES: This is a virtual meeting. Meeting times are tentative and subject to change. The confirmed meeting times, agenda items, and meeting materials including instructions for accessing the live meeting broadcast will be available on the CLIAC website at *www.cdc.gov/cliac.*

FOR FURTHER INFORMATION CONTACT: Nancy Anderson, MMSc, MT(ASCP), Senior Advisor for Clinical Laboratories, Division of Laboratory Systems, Center for Surveillance, Epidemiology and Laboratory Services, Office of Public Health Scientific Services, Centers for Disease Control and Prevention, 1600 Clifton Road, NE, Mailstop V24–3, Atlanta, Georgia 30329–4018, Telephone: (404) 498–2741; Email: *NAnderson@cdc.gov.*

SUPPLEMENTARY INFORMATION:

Purpose: This Committee is charged with providing scientific and technical advice and guidance to the Secretary, HHS; the Assistant Secretary for Health; the Director, CDC; the Commissioner, Food and Drug Administration (FDA); and the Administrator, Centers for Medicare and Medicaid Services (CMS). The advice and guidance pertain to general issues related to improvement in clinical laboratory quality and laboratory medicine practice and specific questions related to possible revision of the Clinical Laboratory Improvement Amendments of 1988 (CLIA) standards. Examples include providing guidance on studies designed to improve safety, effectiveness, efficiency, timeliness, equity, and patient-centeredness of laboratory services; revisions to the standards under which clinical laboratories are regulated; the impact of proposed revisions to the standards on medical and laboratory practice; and the modification of the standards and provision of non-regulatory guidelines to accommodate technological advances, such as new test methods, the electronic transmission of laboratory information, and mechanisms to improve the integration of public health and clinical laboratory practices.

Matters To Be Considered: The agenda will include agency updates from CDC, CMS, and FDA. The focus of the meeting is Clinical Laboratory Medicine in the Age of COVID–19 and will include presentations and discussions on preparedness and response: the partnership between clinical laboratories and public health; laboratory data exchanges during COVID–19; and the clinical laboratory's role in identifying health inequities during the COVID–19 response. Agenda items are subject to change as priorities dictate.

It is the policy of CLIAC to accept written public comments and provide a brief period for oral public comments pertinent to agenda items.

Procedure for Public Comment: Public comment periods for each agenda item are scheduled immediately prior to the Committee discussion period for that item. In general, each individual or group requesting to present an oral comment will be limited to a total time of five minutes (unless otherwise indicated). Speakers should email *CLIAC@cdc.gov* or notify the contact person at least 5 business days prior to the meeting date.

Procedure for Written Public Comment: For individuals or groups unable to attend the meeting, CLIAC accepts written comments until the date of the meeting (unless otherwise stated). However, it is requested that comments be submitted at least 5 business days prior to the meeting date so that the comments may be made available to the Committee for their consideration and public distribution. All written comments will be included in the meeting Summary Report posted on the CLIAC website.

The Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention, has been delegated the authority to sign **Federal Register** notices pertaining to announcements of meetings and other committee management activities, for both the Centers for Disease Control and Prevention and the Agency for Toxic Substances and Disease Registry.

Kalwant Smagh,

Director, Strategic Business Initiatives Unit, Office of the Chief Operating Officer, Centers for Disease Control and Prevention.

[FR Doc. 2020–20182 Filed 9–11–20; 8:45 am]

BILLING CODE 4163–18–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Food and Drug Administration

[Docket No. FDA–2019–E–1943]

Determination of Regulatory Review Period for Purposes of Patent Extension; TAKHZYRO

AGENCY: Food and Drug Administration, Health and Human Services (HHS).

ACTION: Notice.

SUMMARY: The Food and Drug Administration (FDA or the Agency) has determined the regulatory review period for TAKHZYRO and is publishing this notice of that determination as required by law. FDA has made the determination because of the submission of an application to the Director of the U.S. Patent and Trademark Office (USPTO), Department of Commerce, for the extension of a patent which claims that human biological product.

DATES: Anyone with knowledge that any of the dates as published (see **SUPPLEMENTARY INFORMATION**) are incorrect may submit either electronic or written comments and ask for a redetermination by November 13, 2020. Furthermore, any interested person may petition FDA for a determination regarding whether the applicant for extension acted with due diligence during the regulatory review period by March 15, 2021. See ''Petitions'' in the **SUPPLEMENTARY INFORMATION** section for more information.

ADDRESSES: You may submit comments as follows. Please note that late, untimely filed comments will not be considered. Electronic comments must be submitted on or before November 13, 2020. The *https://www.regulations.gov* electronic filing system will accept comments until 11:59 p.m. Eastern Time at the end of November 13, 2020. Comments received by mail/hand delivery/courier (for written/paper submissions) will be considered timely if they are postmarked or the delivery service acceptance receipt is on or before that date.

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–E–1943 for ''Determination of Regulatory Review Period for Purposes of Patent Extension; TAKHZYRO.'' Received comments, those filed in a timely manner (see **ADDRESSES**), 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, 240–402–7500.

• 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 § 10.20 (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.govinfo.gov/content/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, 240–402–7500.

FOR FURTHER INFORMATION CONTACT: Beverly Friedman, Office of Regulatory Policy, Food and Drug Administration, 10903 New Hampshire Ave., Bldg. 51, Rm. 6250, Silver Spring, MD 20993, 301–796–3600.

SUPPLEMENTARY INFORMATION:

I. Background

The Drug Price Competition and Patent Term Restoration Act of 1984 (Pub. L. 98–417) and the Generic Animal Drug and Patent Term Restoration Act (Pub. L. 100–670) generally provide that a patent may be extended for a period of up to 5 years so long as the patented item (human drug product, animal drug product, medical device, food additive, or color additive) was subject to regulatory review by FDA before the item was marketed. Under these acts, a product's regulatory review period forms the basis for determining the amount of extension an applicant may receive.

A regulatory review period consists of two periods of time: A testing phase and an approval phase. For human biological products, the testing phase begins when the exemption to permit the clinical investigations of the biological product becomes effective and runs until the approval phase begins. The approval phase starts with the initial submission of an application to market the human biological product and continues until FDA grants permission to market the biological product. Although only a portion of a regulatory review period may count toward the actual amount of extension that the Director of USPTO may award (for example, half the testing phase must be subtracted as well as any time that may have occurred before the patent was issued), FDA's determination of the length of a regulatory review period for a human biological product will include all of the testing phase and approval phase as specified in 35 U.S.C. 156(g)(1)(B).

FDA has approved for marketing the human biologic product TAKHZYRO (lanadelumab-flyo). TAKHZYRO is indicated for prophylaxis to prevent hereditary angioedema in patients 12 years and older. Subsequent to this approval, the USPTO received a patent term restoration application for TAKHZYRO (U.S. Patent No. 8,816,055) from Dyax Corp., and the USPTO requested FDA's assistance in determining this patent's eligibility for patent term restoration. In a letter dated June 21, 2019, FDA advised the USPTO that this human biological product had undergone a regulatory review period and that the approval of TAKHZYRO represented the first permitted commercial marketing or use of the product. Thereafter, the USPTO requested that FDA determine the product's regulatory review period.

II. Determination of Regulatory Review Period

FDA has determined that the applicable regulatory review period for TAKHZYRO is 1,857 days. Of this time, 1,616 days occurred during the testing phase of the regulatory review period, while 241 days occurred during the approval phase. These periods of time were derived from the following dates:

1. *The date an exemption under section 505(i) of the Federal Food, Drug, and Cosmetic Act (21 U.S.C. 355(i)) became effective:* July 25, 2013. The applicant claims August 2, 2013, as the date the investigational new drug application (IND) became effective. However, FDA records indicate that the IND effective date was July 25, 2013, which was 30 days after FDA receipt of the IND.

2. *The date the application was initially submitted with respect to the human biological product under section 351 of the Public Health Service Act (42 U.S.C. 262):* December 26, 2017. FDA has verified the applicant's claim that the biologics license application (BLA) for TAKHZYRO (BLA 761090) was initially submitted on December 26, 2017.

3. *The date the application was approved:* August 23, 2018. FDA has verified the applicant's claim that BLA 761090 was approved on August 23, 2018.

This determination of the regulatory review period establishes the maximum potential length of a patent extension. However, the USPTO applies several statutory limitations in its calculations of the actual period for patent extension. In its application for patent extension, this applicant seeks 849 days of patent term extension.

III. Petitions

Anyone with knowledge that any of the dates as published are incorrect may submit either electronic or written comments and, under 21 CFR 60.24, ask for a redetermination (see **DATES**). Furthermore, as specified in § 60.30 (21 CFR 60.30), any interested person may petition FDA for a determination regarding whether the applicant for extension acted with due diligence during the regulatory review period. To meet its burden, the petition must comply with all the requirements of § 60.30, including but not limited to: Must be timely (see **DATES**), must be filed in accordance with § 10.20, must contain sufficient facts to merit an FDA investigation, and must certify that a true and complete copy of the petition has been served upon the patent applicant. (See H. Rept. 857, part 1, 98th Cong., 2d sess., pp. 41–42, 1984.) Petitions should be in the format specified in 21 CFR 10.30.

Submit petitions electronically to *https://www.regulations.gov* at Docket No. FDA–2013–S–0610. Submit written petitions (two copies are required) to the Dockets Management Staff (HFA–305), Food and Drug Administration, 5630 Fishers Lane, Rm. 1061, Rockville, MD 20852.

Dated: September 4, 2020.

Lowell J. Schiller,

Principal Associate Commissioner for Policy.

[FR Doc. 2020–20104 Filed 9–11–20; 8:45 am]

BILLING CODE 4164–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

[Document Identifier: OS–0990–0421]

Agency Information Collection Request. 30-Day Public Comment Request

AGENCY: Office of the Secretary, HHS.

ACTION: Notice.

SUMMARY: In compliance with the requirement of the Paperwork Reduction Act of 1995, the Office of the Secretary (OS), Department of Health and Human Services, is publishing the

following summary of a proposed collection for public comment.

DATES: Comments on the ICR must be received on or before October 14, 2020.

ADDRESSES: Written comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *www.reginfo.gov/public/do/PRAMain.* Find this particular information collection by selecting ''Currently under 30-day Review—Open for Public Comments'' or by using the search function.

FOR FURTHER INFORMATION CONTACT: Sherrette Funn, *Sherrette.Funn@hhs.gov* or (202) 795–7714. When submitting comments or requesting information, please include the document identifier 0990–New–30D and project title for reference.

SUPPLEMENTARY INFORMATION: Interested persons are invited to send comments regarding this burden estimate or any other aspect of this collection of information, including any of the following subjects: (1) The necessity and utility of the proposed information collection for the proper performance of the agency's functions; (2) the accuracy of the estimated burden; (3) ways to enhance the quality, utility, and clarity of the information to be collected; and (4) the use of automated collection techniques or other forms of information technology to minimize the information collection burden.

Title of the Collection: ASPE Generic Clearance for the Collection of Qualitative Research and Assessment.

Type of Collection: Extension.

OMB No. 0990–0421—Office of the Assistant Secretary for Planning and Evaluation (ASPE).

Abstract: The Office of the Assistant Secretary for Planning and Evaluation (ASPE) is requesting a three-year extension for their generic clearance for purposes of conducting qualitative research. The ICR is for an extension of the approved information collection assigned OMB control number 0990–0421, scheduled to expire on October 31, 2020. ASPE conducts qualitative research to gain a better understanding of emerging health and human services policy issues, develop future intramural and extramural research projects, and to ensure HHS leadership, agencies and offices have recent data and information to inform program and policy decision-making. ASPE is requesting approval for at least four types of qualitative research which include, but are not limited to: (a) Interviews, (b) focus groups, (c) questionnaires, and (d) other qualitative methods.

ASPE's mission is to advise the Secretary of the Department of Health and Human Services on policy development in health, disability, human services, data, and science, and provides advice and analysis on economic policy. ASPE leads special initiatives, coordinates many of the Department's evaluation, research and demonstration activities, and manages cross-Department planning activities such as implementation of the Evidence Act, strategic planning, legislative planning, and review of regulations. Integral to this role, ASPE will use this mechanism to conduct qualitative research, evaluation, or assessment, conduct analyses, and understand needs, barriers, or facilitators for HHS-related programs and services.

ASPE is requesting comment on the burden for qualitative research aimed at understanding emerging health and human services policy issues. The goal of developing these activities is to identify emerging issues and research gaps to ensure the successful implementation of HHS programs. The participants may include health and human services experts; national, state, and local health or human services representatives; public health, human services, or healthcare providers; and representatives of other health or human services organizations.

Need and Proposed Use of the Information: ASPE is requesting comment on the burden for qualitative research aimed at understanding emerging health and human services policy issues. The goal of developing these activities is to identify emerging issues and research gaps to ensure the successful implementation of HHS programs. The participants may include health and human services experts; national, state, and local health or human services representatives; public health, human services, or healthcare providers; and representatives of other health or human services organizations. The increase in burden from 747 in 2014 to 1,300 respondents in 2017 reflects an increase in the number of research projects conducted over the estimate in 2014. There is no change in request of burden hours from 2017 to 2020.

The total annual burden hours estimated for this ICR are summarized in the table below.

ESTIMATED ANNUALIZED BURDEN TABLE

Type of respondent	Form	Number of respondents	Number of responses per respondent	Average burden hours per response	Total burden hours
Health or Human Services Policy Stakeholder	Qualitative Research	1,300	1	1	1,300

Sherrette A. Funn,

Office of the Secretary, Paperwork Reduction Act Reports Clearance Officer.

[FR Doc. 2020–20136 Filed 9–11–20; 8:45 am]

BILLING CODE 4151–05–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Cancer Institute; Amended Notice of Meeting

Notice is hereby given of a change in the meeting of the National Cancer Institute Council of Research Advocates, September 14, 2020, 12:00 p.m. to September 14, 2020, 4:00 p.m., National Institutes of Health, Building 31, 9000 Rockville Pike, Bethesda, MD 20892 which was published in the **Federal Register** on August 14, 2020, 85 FR 49663.

This meeting notice is amended to change the meeting start time. The meeting will now be held from 1:00 p.m. to 4:00 p.m. on September 14, 2020. The meeting is open to the public.

Dated: September 8, 2020.

Melanie J. Pantoja,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–20119 Filed 9–11–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

National Institutes of Health

National Human Genome Research Institute; Notice of Closed Meeting

Pursuant to section 10(d) of the Federal Advisory Committee Act, as amended, notice is hereby given of a meeting of the Board of Scientific Counselors, National Human Genome Research Institute.

The meeting will be closed to the public as indicated below in accordance with the provisions set forth in section 552b(c)(6), Title 5 U.S.C., as amended for the review, discussion, and evaluation of individual grant applications conducted by the NATIONAL HUMAN GENOME RESEARCH INSTITUTE, including consideration of personnel qualifications and performance, and the competence of individual investigators, the disclosure of which would constitute a clearly unwarranted invasion of personal privacy.

Name of Committee: Board of Scientific Counselors, National Human Genome Research Institute.

Date: December 1–2, 2020.

Time: 8:00 a.m. to 5:00 p.m.

Agenda: To review and evaluate personnel qualifications and performance, and competence of individual investigators.

Place: National Human Genome Research Institute, National Institutes of Health, Building 50, Room 5222C, Bethesda, MD 20892 (Virtual Meeting).

Contact Person: Paul Liu, Ph.D., MD, Deputy Scientific Director, National Human Genome Research Institute, National Institutes of Health, Building 50, Room 5222C, Bethesda, MD 20892, (301) 402–2529, *pliu@mail.nih.gov.*

(Catalogue of Federal Domestic Assistance Program Nos. 93.172, Human Genome Research, National Institutes of Health, HHS)

Dated: September 8, 2020.

Melanie J. Pantoja,

Program Analyst, Office of Federal Advisory Committee Policy.

[FR Doc. 2020–20120 Filed 9–11–20; 8:45 am]

BILLING CODE 4140–01–P

DEPARTMENT OF HOMELAND SECURITY

Federal Emergency Management Agency

[Docket ID: FEMA–2020–0030; OMB No. 1660–0002]

Agency Information Collection Activities: Proposed Collection; Comment Request; Disaster Assistance Registration

AGENCY: Federal Emergency Management Agency, DHS.

ACTION: 60-Day notice and request for comments.

SUMMARY: The Federal Emergency Management Agency, as part of its continuing effort to reduce paperwork and respondent burden, invites the general public to take this opportunity to comment on a revision of a currently approved information collection. In accordance with the Paperwork Reduction Act of 1995, this notice seeks comments concerning Disaster Assistance Registration.

DATES: Comments must be submitted on or before November 13, 2020.

ADDRESSES: To avoid duplicate submissions to the docket, please use the following means to submit comments:

Online. Submit comments at *www.regulations.gov* under Docket ID FEMA–2020–0030 Follow the instructions for submitting comments.

All submissions received must include the agency name and Docket ID. All submissions will be posted, without change, to the Federal eRulemaking Portal at *http://www.regulations.gov,* and will include any personal information you provide. Therefore, submitting this information makes it public. You may wish to read the Privacy and Security Notice that is available via a link on the homepage of *www.regulations.gov.*

FOR FURTHER INFORMATION CONTACT: Brian Thompson, Supervisory Program Specialist, FEMA, Recovery Directorate, *Brian.Thompson6@fema.dhs.gov,* 540–686–3602. You may contact the Information Management Division for copies of the proposed collection of information at email address: *FEMA-Information-Collections-Management@fema.dhs.gov.*

SUPPLEMENTARY INFORMATION: The Robert T. Stafford Disaster Relief and Emergency Assistance Act (Pub. L. 93–288, 42 U.S.C. 5121, *et seq.*) (the Stafford Act), as amended, is the legal basis for the Federal Emergency Management Agency (FEMA) to provide financial assistance and services to individuals who apply for disaster assistance benefits in the event of a federally-declared disaster. Title 44 CFR, Part 206, Subpart D, ''Federal Assistance to Individuals and Households,'' provides the regulatory framework implementing the policy and procedures set forth in § 408 of the Stafford Act. This program provides financial assistance and, if necessary, direct assistance to eligible individuals and households who, as a direct result of a major disaster, have necessary expenses and serious needs that are unable to be met through other means. Individuals and households may apply for assistance (Registration Intake) under the Individuals and Households program in person, via telephone, or internet.

Collection of Information

Title: Disaster Assistance Registration.

Type of Information Collection: Revision of a currently approved information collection.

OMB Number: 1660–0002.

FEMA Forms: FEMA Form 009–0–1T (English) Tele-Registration, Disaster Assistance Registration; FEMA Form 009–0–1Int (English) internet, Disaster Assistance Registration; FEMA Form 009–0–2Int (Spanish) internet, Registro Para Asistencia De Desastre; FEMA Form 009–0–1 (English) Paper Application, Disaster Assistance Registration; FEMA Form 009–0–2 (Spanish), Solicitud en Papel, Registro Para Asistencia De Desastre; FEMA Form 009–0–3 (English), Declaration and Release; FEMA Form 009–0–4 (Spanish), Declaración Y Autorización; FEMA Form 009–0–5 (English), Manufactured Housing Unit Revocable License and Receipt for Government Property; FEMA Form 009–0–6 (Spanish), Las Casas Manufacturadas Unidad Licencia Revocable y Recibo de la Propiedad del Gobierno; Request for Information.

Abstract: The forms in this collection are used to obtain pertinent information to provide financial assistance, and if necessary, direct assistance to eligible individuals and households who, as a direct result of a disaster or emergency, have uninsured or under-insured, necessary or serious expenses they are unable to meet. To provide meaningful access to individuals with disabilities throughout FEMA programs, the revision to the collection will obtain pertinent disability-related information.

Affected Public: Individuals or Households.

Estimated Number of Respondents: 1,004,488.

Estimated Number of Responses: 1,004,488.

Estimated Total Annual Burden Hours: 356,007.

Estimated Total Annual Respondent Cost: $13,368,063.

Estimated Respondents' Operation and Maintenance Costs: $0.

Estimated Respondents' Capital and Start-Up Costs: $0.

Estimated Total Annual Cost to the Federal Government: $32,192,627.

Comments

Comments may be submitted as indicated in the **ADDRESSES** caption above. Comments are solicited to (a) evaluate whether the proposed data collection is necessary for the proper performance of the agency, including whether the information shall have practical utility; (b) 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; (c) enhance the quality, utility, and clarity of the information to be collected; and (d) 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.

Maile Arthur,

Deputy Director of Information Management, Mission Support, Federal Emergency Management Agency, Department of Homeland Security.

[FR Doc. 2020–20191 Filed 9–11–20; 8:45 am]

BILLING CODE 9111–23–P

DEPARTMENT OF THE INTERIOR

Bureau of Indian Affairs

[201A2100DD/AAKC001030/ A0A501010.999900 253G]

Advisory Board for Exceptional Children

AGENCY: Bureau of Indian Affairs, Interior.

ACTION: Notice of Meeting.

SUMMARY: The Bureau of Indian Education (BIE) is announcing that the Advisory Board for Exceptional Children is holding an upcoming meeting to meet the mandates of the Individuals with Disabilities Education Act of 2004 (IDEA) for Indian children with disabilities. Due to the COVID–19 pandemic and for the safety of all individuals, the meeting will be held online. DATES: The BIE Advisory Board meeting will be held Wednesday, September 30, 2020 from 8 a.m. to 3:30 p.m. Pacific Daylight Time (PDT).

ADDRESSES: All Advisory Board activities and meetings will be conducted online. See the **SUPPLEMENTARY INFORMATION** section of this notice for directions on joining. Public comments can also be emailed to the DFO at *Jennifer.davis@indianaffairs.gov;* or faxed to (602) 265–0293 Attention: Jennifer Davis, DFO; or mailed or hand delivered to the Bureau of Indian Education, Attention: Jennifer Davis, DFO, 2600 N Central Ave. Suite 800, Phoenix, AZ 85004.

FOR FURTHER INFORMATION CONTACT: Jennifer Davis, Designated Federal Officer, Bureau of Indian Education, 2600 N Central Ave. Suite 800, Phoenix, AZ 85004, email at *Jennifer.davis@indianaffairs.gov* or telephone numbers (202) 860–7845 or (602) 240–8597.

SUPPLEMENTARY INFORMATION: In accordance with the Federal Advisory Committee Act, the BIE is announcing that the Advisory Board will hold its next meeting online. The Advisory Board was established under the Individuals with Disabilities Act of 2004 (20 U.S.C. 1400 *et seq.*) to advise the Secretary of the Interior, through the Assistant Secretary-Indian Affairs, on the needs of Indian children with disabilities. The meeting is open to the public.

The following items will be on the agenda:

• Navajo Region Schools—Special Education Update Report.

• Work on 2020 Annual Report.

• Public Comments (via teleconference call, Wednesday, September 30, 2020).

How to Join the Meeting

You can join the meeting in any of the following ways:

• From your computer, tablet or smartphone * using *https://global.gotomeeting.com/join/940105053;* or

• Dial in using your phone, United States: +1 (571) 317–3122 and Access Code: 940–105–053; or

• From a video-conferencing room or system by dialing in or typing: 67.217.95.2 or *inroomlink.goto.com,* Meeting ID: 940 105 053, or dialing directly: 940105053@67.217.95.2 or 67.217.95.2##940105053.

* If you are new to GoToMeeting you can get the app by using this link: *https://global.gotomeeting.com/install/940105053.*

Opportunity for Public To Comment

During the September 30, 2020 meeting, time has been set aside for public comments via webinar or telephone conference call from 9:15 p.m. to 9:45 p.m. Pacific Daylight Time. To join the meeting, follow the directions listed above. You may also submit comments in writing to the individual listed in the **ADDRESSES** section of this notice.

Authority

This notice is published under the authority of 5 U.S.C. Appendix 5; 20 U.S.C. 1400 *et seq.*

Tara Sweeney,

Assistant Secretary, Indian Affairs.

[FR Doc. 2020–20185 Filed 9–11–20; 8:45 am]

BILLING CODE 4337–15–P

DEPARTMENT OF THE INTERIOR

Bureau of Indian Affairs

[201A2100DD/AAKC001030/ A0A501010.999900 253G]

Annual Meeting Under Indian Employment, Training and Related Services Act, as Amended

AGENCY: Bureau of Indian Affairs, Interior.

ACTION: Notice of Meeting.

SUMMARY: The Department of the Interior, Bureau of Indian Affairs (BIA), is announcing the annual meeting of the Federal agencies and Tribes that participate in the Indian Employment, Training and Related Services Act of 2017, also known as ''Public Law 477.'' Due to the COVID–19 pandemic and for the safety of all individuals, the meeting will be conducted via WebEx and by telephone.

DATES: The annual Federal Partner and Tribal 477 Work Group meeting will be held on Monday, September 28, 2020 from 12:30 p.m. to 3:30 p.m. Eastern Daylight Time (EDT).

ADDRESSES: All Advisory Board activities and meetings will be conducted online and by phone. See the **SUPPLEMENTARY INFORMATION** section of this notice for directions to join WebEx and by telephone.

FOR FURTHER INFORMATION CONTACT: Jeanette Hanna, Deputy Bureau Director, Indian Services, Bureau of Indian Affairs, *Jeanette.Hanna@bia.gov,* (202) 513–7640.

SUPPLEMENTARY INFORMATION: The annual Federal Partner and Tribal 477 Work Group meeting will be on WebEx video conference and by phone. Call-in information follows:

WebEx: https://ocfoia.webex.com/ocfoia/onstage/g.php?MTID=ef573c94c1da637700998e9ffe034741a
Call in: +1–415–527–5035
Access code: 199 196 6375

Background

In 2017, the Congress enacted the Indian Employment Training and Related Services Consolidation Act of 2017, Public Law 115–93, codified at 25 U.S.C. 3401–3417 (''2017 Act''). The 2017 update amended and expanded the Indian Employment and Related Services Demonstration Act of 1992, Public Law 102–477 (as amended in 2017, ''PL 477'') by, in part, identifying eight additional Federal agencies that are now subject to the amended law, including the Departments of Justice, Agriculture, Commerce, Energy, Homeland Security, Housing and Urban Development, Transportation, and Veterans Affairs. Under PL 477, Tribes may propose to integrate eligible grant programs from these agencies and the Departments of the Interior, Health and Human Services, Labor and Education, consolidate and reprogram grant funds in accordance with a plan approved by the Secretary of the Interior (''477 Plan''). As required by the 2017 updates to PL 477, the Department of the Interior entered into a Memorandum of Agreement (MOA) among the 12 Federal agencies to implement PL 477.

Annual Meeting

As lead agency responsible for implementation of PL 477, BIA announces the annual meeting of participating Tribes and Federal agencies. As directed by statute, the meeting will be co-chaired by Assistant Secretary-Indian Affairs Tara Sweeney and 477 Tribal Work Group Committee Chair Margaret Zientek. 25 U.S.C. 3410(a)(3)(B)(i).

The agenda will include:

I. Status of Participating 477 Tribes
- 477 Programs to be integrated
- Plan Approval Process
- Waiver Approvals
- Funds Transfer
- Annual Reports
- 477 Tribal Recognitions

II. Discussion on Memorandum of Agreement
- Status of Memorandum of Agreement
- Recommendation for Changes/Improvements/Areas to be addressed
- Status of Labor Force Report

III. COVID–19 Pandemic
- Challenges and Success

IV. Miscellaneous
- Financial Assistance for 477 Tribes to develop a database
- Expansion of Tribal programs
- Establish Annual Meeting of Tribes and Federal agencies

To join the meeting, use WebEx video call or call in by phone:

WebEx: https://ocfoia.webex.com/ocfoia/onstage/g.php?MTID=ef573c94c1da637700998e9ffe034741a
Call in: +1–415–527–5035
Access code: 199 196 6375

Tara Sweeney,
Assistant Secretary—Indian Affairs.

[FR Doc. 2020–20186 Filed 9–11–20; 8:45 am]

BILLING CODE 4337–15–P

DEPARTMENT OF THE INTERIOR

Bureau of Land Management

[LLCON01000.L14400000.EU0000.20X]

Notice of Realty Action: Segregation of Public Land for Proposed Non-Competitive (Direct) Sale in Moffat County, CO

AGENCY: Bureau of Land Management, Interior.

ACTION: Notice of realty action.

SUMMARY: The Bureau of Land Management (BLM) is proposing a non-competitive (direct) sale of 2.13 acres of public land in Moffat County to the Moffat County Board of County Commissioners to resolve an inadvertent, unauthorized use of public lands. The sale will be subject to the applicable provisions of the Federal Land Policy and Management Act of 1976 (FLMPA), as amended, and BLM land sale regulations. The sale will be for no less than the appraised fair market value (FMV).

DATES: Interested parties must submit written comments no later than October 29, 2020.

ADDRESSES: Mail written comments to Bruce Sillitoe, Field Manager, BLM Little Snake River Field Office, 455 Emerson Street, Craig, CO 81625.

FOR FURTHER INFORMATION CONTACT: Janell Corey, Realty Specialist, BLM Little Snake Field Office, at the previous address, or by telephone at 970–826–5053, or by email at *jcorey@blm.gov.* Persons who use a telecommunications device for the deaf (TDD) may call the Federal Relay Service (FRS) at 1–800–877–8339 to contact Ms. Corey during normal business hours. The FRS is available 24 hours a day, 7 days a week, to leave a message or questions. You will receive a reply during normal business hours.

SUPPLEMENTARY INFORMATION: The Moffat County Board of County Commissioners formally requested to purchase the subject parcel to resolve its inadvertent, unauthorized use.

The following described public lands in Moffat County are segregated from all forms of appropriation under public laws, including the mining laws, upon publication of this notice:

Sixth Principal Meridian, Colorado

T. 9 N., R. 102 W.,
sec. 2, lot 36;
sec. 3, lot 24.
The area described contains 2.13 acres.

The BLM is no longer accepting applications affecting the subject parcel, except those to amend previously filed right-of-way applications or the existing authorization to increase grant terms in accordance with 43 CFR 2807.15 and 2886.15.

During the segregation period, the BLM will conduct a parcel-specific environmental analysis and review in accordance with the Secretarial Order 3373—*Evaluating Public Access in Bureau of Land Management Public Land Disposals and Exchanges,* to determine any adverse effects before offering the subject parcel for sale.

The segregation will terminate upon issuance of a patent, publication in the **Federal Register** for termination of the segregation, or September 14, 2022, unless extended prior to the termination date by the BLM Colorado State Director in accordance with 43 CFR 2711.1–2(d).

The proposed sale is in conformance with the BLM Little Snake Resource Management Plan (RMP), approved in October 2011, on page RMP–52 and Management Action: Allowable Uses and Actions. The Authorized Officer has determined this sale to be in the best interest of the public in accordance with the provisions of the RMP.

Existing historical structures make the subject parcel difficult for the BLM to manage. Under FLPMA Section 203, disposal of the subject parcel is allowed because existing characteristics are difficult and uneconomic to manage and the parcel is not suitable for management by another Federal department or agency.

In accordance with 43 CFR 2710–0–6 and 43 CFR 2711.3–3(a), ''Direct sales (without competition) may be utilized, when in the opinion of the authorized officer, a competitive sale is not appropriate and the public interest would best be served by a direct sale.'' In this case, a direct sale is appropriate because the subject parcel contains previously and inadvertently built, unauthorized historical structures significant to the history of public schools in Moffat County. The county intends to use the property for public education and to enhance tourism in the area.

The BLM considered the minimal acreage to create a manageable boundary to include lands needed to protect existing improvements and to resolve the inadvertent, unauthorized use. The BLM may serve the public's interest through resolution and receiving payment at FMV for the subject parcel.

If issued, the conveyance document will be subject to valid existing rights and encumbrances of record, including, but not limited to, rights-of-way for roads and public utilities, and reservations for ditches and canals and all mineral deposits.

In addition to this Notice of Realty Action, a sale notice will be published once a week for 3 weeks in the *Craig Daily Press.* Only written comments submitted by mail will be considered as properly filed. Electronic mail, facsimile, or verbal comments will not be considered.

Before including your address, phone number, email address, or other personal identifying information (PII) in your comment, you should be aware that your comment, including your PII, may be made publicly available at any time. While you may ask us in your comment to withhold your PII from public review, the BLM cannot guarantee that it will be able to do so.

Any adverse comments will be reviewed by the BLM Colorado State Director or other authorized official of the Department of the Interior, who may sustain, vacate, or modify this realty action in whole or in part. In the absence of timely filed objections, this realty action will become the final determination of the Department of the Interior.

(Authority: 43 CFR 2091.2–1(b))

Jamie E. Connell,

Colorado State Director.

[FR Doc. 2020–20114 Filed 9–11–20; 8:45 am]

BILLING CODE 4310–HC–P

DEPARTMENT OF THE INTERIOR

National Park Service

[NPS–WASO–NRNHL–DTS#-30831; PPWOCRADI0, PCU00RP14.R50000]

National Register of Historic Places; Notification of Pending Nominations and Related Actions

AGENCY: National Park Service, Interior.

ACTION: Notice.

SUMMARY: The National Park Service is soliciting electronic comments on the significance of properties nominated before August 29, 2020, for listing or related actions in the National Register of Historic Places.

DATES: Comments should be submitted electronically by September 29, 2020.

ADDRESSES: Comments are encouraged to be submitted electronically to *National_Register_Submissions@nps.gov* with the subject line ''Public Comment on <property or proposed district name, (County) State>.'' If you have no access to email you may send them via U.S. Postal Service and all other carriers to the National Register of Historic Places, National Park Service, 1849 C Street NW, MS 7228, Washington, DC 20240.

SUPPLEMENTARY INFORMATION: The properties listed in this notice are being considered for listing or related actions in the National Register of Historic Places. Nominations for their consideration were received by the National Park Service before August 29, 2020. Pursuant to Section 60.13 of 36 CFR part 60, comments are being accepted concerning the significance of the nominated properties under the National Register criteria for evaluation.

Before including your address, phone number, email address, or other personal identifying information in your comment, you should be aware that your entire comment—including your personal identifying information—may be made publicly available at any time. While you can ask us in your comment to withhold your personal identifying information from public review, we cannot guarantee that we will be able to do so.

Nominations submitted by State or Tribal Historic Preservation Officers:

ILLINOIS

Mercer County

Verdurette, 665 65th Ave. New Boston, SG100005658

IOWA

Muscatine County

Leith, Doctor Alexander R. (A.R.) and Louisa J., House, 117 West 6th St., Wilton, SG100005657

MARYLAND

Charles County

Moyaone Reserve Historic District, Roughly bounded by Bryan Point Rd., Piscataway Park, Overlook Dr./Old Landing Rd., and Farmington Rd. West, Bryans Road vicinity, SG100005659

Prince George's County

Moyaone Reserve Historic District, Roughly bounded by Bryan Point Rd., Piscataway Park, Overlook Dr./Old Landing Rd., and Farmington Rd. West, ≤Accokeek vicinity, SG100005659

MISSOURI

Jackson County

East Ninth Street-Grand Boulevard Historic District, Roughly bounded by Main, McGee, East 8th and East 10th Sts., Kansas City, SG100005660

Community Church, 4601 Main St., Kansas City, SG100005662

Wheatley-Provident Hospital, 1826 Forest Ave., Kansas City, SG100005665

Miller County

Grand Auglaize Bridge, Swinging Bridges Rd. across Grand Auglaize Cr., Brumley vicinity, SG100005663

St. Louis County

Bank of St. Ann, 10449 St. Charles Rock Rd., St. Ann, SG100005661

St. Louis Independent City, Metropolitan Police Garage, 3919 Laclede Ave., St. Louis, SG100005664

PENNSYLVANIA

Erie County

Orton, Almerion C. & Barbara Moseman, Farm (Agricultural Resources of Pennsylvania c1700–1960 MPS), 7853 Knoyle Rd., Wattsburg, MP100005655

Monroe County

Parkside Chapel, 5335 Paradise Valley Rd., Henryville, SG100005656

Philadelphia County

Edward Corner Marine Merchandise Warehouse, 1100–1102 North Delaware Ave., Philadelphia, SG100005654

VERMONT

Windsor County

Park Street School (Educational Resources of Vermont MPS), 60 Park St., Springfield, MP100005653

Authority: Section 60.13 of 36 CFR part 60.

Dated: September 1, 2020.

Sherry A. Frear,

Chief, National Register of Historic Places/ National Historic Landmarks Program.

[FR Doc. 2020–20188 Filed 9–11–20; 8:45 am]

BILLING CODE 4312–52–P

INTERNATIONAL TRADE COMMISSION

[Investigation No. 337–TA–1174]

Certain Toner Cartridges, Components Thereof, and Systems Containing Same; Commission Determination Not To Review an Initial Determination Granting Complainants' Motion for Summary Determination of a Violation of Section 337; Schedule for Filing Written Submissions on Remedy, the Public Interest, and Bonding

AGENCY: U.S. International Trade Commission.

ACTION: Notice.

SUMMARY: Notice is hereby given that, on July 23, 2020, the presiding administrative law judge (''ALJ'') issued an initial determination (''ID'') (Order No. 40) in the above-captioned investigation, granting summary determination on violation of section 337 and including a recommended determination (''RD'') on remedy and bonding. The Commission has determined not to review the ID. The Commission requests briefing from the parties, interested government agencies, and interested persons on the issues of remedy, the public interest, and bonding.

FOR FURTHER INFORMATION CONTACT: Panyin A. Hughes, Office of the General Counsel, U.S. International Trade Commission, 500 E Street SW, Washington, DC 20436, telephone (202) 205–3179. Copies of non-confidential documents filed in connection with this investigation may be viewed on the Commission's electronic docket (EDIS) at *https://edis.usitc.gov.* For help accessing EDIS, please email *EDIS3Help@usitc.gov.* General information concerning the Commission may also be obtained by accessing its internet server at *https://www.usitc.gov.* Hearing-impaired persons are advised that information on this matter can be obtained by contacting the Commission's TDD terminal, telephone (202) 205–1810.

SUPPLEMENTARY INFORMATION: On September 17, 2019, the Commission instituted this investigation based on a complaint filed by Brother Industries, Ltd. of Nagoya Japan; Brother International Corp. (U.S.A.) of Bridgewater, New Jersey; and Brother Industries (U.S.A.), Inc. of Bartlett, Tennessee (collectively, ''Brother''). 84 FR 49762–63 (Sept. 23, 2019). The complaint alleged violations of section 337 based on the importation into the United States, the sale for importation, or the sale within the United States after importation of certain toner cartridges, components thereof, and systems containing same by reason of infringement of certain claims of U.S. Patent Nos. 9,568,856; 9,575,460; 9,632,456; 9,785,093; and 9,846,387 (collectively, ''the Asserted Patents''). *Id.* The Commission's notice of investigation named the following 32 respondents: AMI Brothers, Inc. of San Bruno, California (''AMI''); An An Beauty Limited of Kowloon, Hong Kong (''An An Beauty''); Aster Graphics, Inc. of Riverside, California (''Aster''); Aztech Enterprises Limited of Kowloon, Hong Kong (''Aztech''); Billiontree Technology USA Inc. of City of Industry, California (''Billiontree''); Carlos Imaging Supplies, Inc. of Hacienda Heights, California (''Carlos''); Cartridge Evolution, Inc. of Brooklyn, New York (''Cartridge Evolution''); Do it Wiser, LLC of Wilmington, Delaware (''Do it Wiser''); Eco Imaging Inc. of Irvine, California (''Eco Imaging''); Ecoolsmart Co. of Rowland Heights, California (''Ecoolsmart''); EPrinter Solution LLC of Pomona, California (''EPS''); E–Z Ink Inc. of Brooklyn, New York (''E–Z Ink''); Globest Trading Inc. of Ontario, California (''Globest''); Greencycle Tech, Inc. of South El Monte, California (''Greencycle''); Hongkong Boze Co., Ltd. of Kowloon, Hong Kong (''Hongkong Boze''); I8 International, Inc. of City of Industry, California (''I8''); IFree E-Commerce Co. of Kowloon, Hong Kong (''IFree''); Ikong E-Commerce of Walnut, California (''Ikong''); Intercon International Corp. of Brea, California (''Intercon''); IPrint Enterprise Limited of Kowloon, Hong Kong (''IPrint''); LD Products, Inc. of Long Beach, California (''LD Products''); Linkyo Corp. of La Puente, California (''Linkyo''); Mangoket LLC of Alhambra, California (''Mangoket''); New Era Image LLC of Corona, California (''New Era''); OW Supplies Corp. of Corona, California (''OW Supplies''); Solong E-Commerce Co., LLC of Wan Chai, Hong Kong (''Solong''); Smartjet E-Commerce Co., LLC of Wan Chai, Hong Kong (''Smartjet''); Super Warehouse Inc. of Blaine, Washington (''Super Warehouse''); Theresa Meng of Brooklyn, New York (''Ms. Meng''); Triple Best LLC of San Diego, California (''Triple Best''); V4ink, Inc. of Diamond Bar, California (''V4ink''); and Zhuhai Xiaohui E-Commerce Co., Ltd. of Zhuhai, China (''Xiaohui''). *Id.* at 49762–63. The notice of investigation also names the Office of Unfair Import Investigations (''OUII'') as a party. *Id.* at 49763.

Of the 32 respondents, only one, Aster, is participating at this stage. Aster, however, decided not to oppose the summary determination motion of violation as to the accused products, even though Aster's products are subject to the motion. *See* Joint Stipulation of Brother and Aster for Resolution as to Aster in the Investigation (Mar. 4, 2020). EPS and IFree were terminated from the investigation based upon withdrawal of the complaint against them. *See* Order No. 32 (Jan. 28, 2020), *unreviewed by* Comm'n Notice (Feb. 25, 2020). Cartridge Evolution, E–Z Ink, Linkyo, New Era, OW Supplies, Ms. Meng, Triple Best, and V4ink were terminated from the investigation based upon entry of consent orders. *See* Order No. 36 (Mar. 12, 2020), *unreviewed by* Comm'n Notice (Mar. 31, 2020); Order No 38 (Mar. 12, 2020), *unreviewed by* Comm'n Notice (Mar. 31, 2020); Order No. 37 (Mar. 12, 2020), *unreviewed by* Comm'n Notice (Mar. 31, 2020); Order No. 10 (Oct. 18, 2019), *unreviewed by* Comm'n Notice (Nov. 6, 2019); Order No. 17 (Nov. 21, 2019), *unreviewed by* Comm'n Notice (Dec. 18, 2019); Order No. 28 (Dec. 30, 2019), *unreviewed by* Comm'n Notice (Jan. 29, 2020); Order No. 18 (Nov. 27, 2019), *unreviewed by* Comm'n Notice (Dec. 18, 2019); Order No. 33 (Fe. 3, 2020), *unreviewed by* Comm'n Notice (Mar. 4, 2020). The following 21 respondents defaulted: AMI, Globest, An An Beauty, Aztech, Xiaohui, Ecoolmart, Greencycle, Intercon, Do it Wiser, I8, Solong, Billiontree, Carlos Imaging, Eco Imaging, Hongkong Boze, Ikong, IPrint, Mangoket, Smartjet, Super Warehouse, and LD Products (collectively, ''Defaulting Respondents''). *See* Order No. 35 (Mar. 5, 2020), *unreviewed by* Comm'n Notice (Mar. 19, 2020); Order No. 31 (Jan. 22, 2020), *unreviewed by* Comm'n Notice (Feb. 21, 2020); Order No. 26 (Dec. 20, 2019), *unreviewed by* Comm'n Notice (Jan 16, 2020); Order No. 25 (Dec. 18, 2019), *unreviewed by* Comm'n Notice (Jan. 16, 2020); Order No. 24 (Dec. 18, 2019), *unreviewed by* Comm'n Notice (Jan. 16, 2020); Order No. 8 (Oct. 15, 2019), *unreviewed by* Comm'n Notice (Nov. 7, 2019).

On March 12, 2020, Brother filed a motion for summary determination of violation of section 337 by Aster and the Defaulting Respondents and for a recommendation that the Commission issue a general exclusion order and cease and desist orders. *See* Complainants' Motion for Summary Determination of Violation and for Recommended Determination on Remedy and Bonding. On March 23, 2020, OUII filled a response in support of Brother's motion. *See* Commission Investigative Staff's Response to Brother's Motion for Summary Determination of Violation. No respondent filed a response to Brother's motion. *Id.*

On July 23, 2020, the ALJ issued the subject ID granting summary determination of violation of section 337 by Aster and Defaulting Respondents. The ID finds that the Commission has subject matter jurisdiction over the investigation. ID at 34. The ID further finds that none of the respondents contest the Commission's personal jurisdiction over them or in rem jurisdiction as to the accused products. ID at 34–35. The ID finds that Brother: (1) Established the importation requirement as to Aster and Defaulting Respondents, ID at 36–79; (2)

demonstrated that the accused products infringe the asserted claims, *id.* at 118–133; and (3) demonstrated that the domestic industry (''DI'') products practice at least one claim of each Asserted Patent and that a DI exists in the United States, *id.* at 84–118. The RD recommends issuance of a general exclusion order (''GEO'') (or, in the alternative, a limited exclusion order directed to Aster and each of the Defaulting Respondents). *Id.* at 134–44. The RD further recommends issuance of cease and desist orders (''CDOs'') directed to Aster and each defaulting respondent that has domestic operations. *Id.* at 144–46. The RD also recommends setting different bond rates for entry of the different products covered by the GEO during the period of Presidential review. *Id.* at 146–48 (recommended bond rate table at 147). No one petitioned for review of the ID.

The Commission has determined not to review the ID.

On August 24, 2020, Aster filed a public interest statement in response to the Commission's notice soliciting public interest comments pursuant to 19 CFR 210.50(a)(4)(i). In its submission, Aster argued that any Commission remedial orders issued in this investigation should not cover its new products pursuant to its stipulation with Brother. *See* Respondent Aster Graphics, Inc.'s Statement of Public Interest. On August 26, 2020, Brother filed a response. *See* Complainants' Motion to Strike Aster Graphics, Inc.'s Statement on the Public Interest for Failure to Comply with Commission Rule 210.15 Or, in the Alternative, for Leave to Respond. The Commission has determined to reject Aster's submission as improper under 19 CFR 210.50(a)(4)(i). 19 CFR 210.50(a)(4)(i) provides that parties may file information with the Commission relating to the public interest. Aster's submission, however, concerns the scope of the remedy and therefore does not fall within the ambit of the public interest submissions provided for under 19 CFR 210.50(a)(4)(i). Brother's response is thereby moot. The Commission notes that Aster will have an opportunity to raise its arguments regarding the scope of any remedial orders in a remedy submission before the Commission in response to the instant notice, which invites parties to file submissions addressing remedy, bonding and the public interest as noted below.

In connection with the final disposition of this investigation, the statute authorizes issuance of: (1) An exclusion order that could result in the exclusion of the subject articles from entry into the United States, and/or (2) one or more cease and desist orders that could result in Aster and the Defaulting Respondents being required to cease and desist from engaging in unfair acts in the importation and sale of such articles. Accordingly, the Commission is interested in receiving written submissions that address the form of remedy, if any, that should be ordered. If a party seeks exclusion of an article from entry into the United States for purposes other than entry for consumption, the party should so indicate and provide information establishing that activities involving other types of entry either are adversely affecting it or likely to do so. For background, *see Certain Devices for Connecting Computers via Telephone Lines,* Inv. No. 337–TA–360, USITC Pub. No. 2843, Comm'n Op. at 7–10 (December 1994).

The statute requires the Commission to consider the effects of any remedy upon the public interest. The public interest factors the Commission will consider include the effect that an exclusion order and/or CDO would have on: (1) The public health and welfare; (2) competitive conditions in the U.S. economy; (3) U.S. production of articles that are like or directly competitive with those that are subject to investigation; and (4) U.S. consumers. The Commission is therefore interested in receiving written submissions that address the aforementioned public interest factors in the context of this investigation.

If the Commission orders some form of remedy, the U.S. Trade Representative, as delegated by the President, has 60 days to approve, disapprove, or take no action on the Commission's determination. *See* Presidential Memorandum of July 21, 2005. 70 FR 43251 (July 26, 2005). During this period, the subject articles would be entitled to enter the United States under bond, in an amount determined by the Commission and prescribed by the Secretary of the Treasury. The Commission is therefore interested in receiving submissions concerning the amount of the bond that should be imposed if a remedy is ordered.

Written Submissions: Parties to this investigation, interested government agencies, and any other interested parties are invited to file written submissions on the issues of remedy, the public interest, and bonding. Such submissions should include views on the recommended determination by the ALJ on remedy and bonding.

In their initial written submissions, Brother is also requested to identify the remedy sought and Brother and OUII are also requested to submit proposed remedial orders for the Commission's consideration. Brother is further requested to identify the dates the Asserted Patents expire, to provide the HTSUS subheadings under which the subject articles are imported, and to supply identification information for all known importers of the subject articles.

Initial written submissions, including proposed remedial orders, must be filed no later than close of business on September 22, 2020. Reply submissions must be filed no later than the close of business on September 29, 2020. No further submissions on any of these issues will be permitted unless otherwise ordered by the Commission.

Persons filing written submissions must file the original document electronically on or before the deadlines stated above. The Commission's paper filing requirements in 19 CFR 210.4(f) are currently waived. 85 FR 15798 (Mar. 19, 2020). Submissions should refer to the investigation number (Inv. No. 337–TA–1174) in a prominent place on the cover page and/or the first page. (*See* Handbook for Electronic Filing Procedures, *https://www.usitc.gov/documents/handbook_on_filing_procedures.pdf*). Persons with questions regarding filing should contact the Secretary (202–205–2000).

Any person desiring to submit a document to the Commission in confidence must request confidential treatment. All such requests should be directed to the Secretary to the Commission and must include a full statement of the reasons why the Commission should grant such treatment. *See* 19 CFR 201.6. Documents for which confidential treatment by the Commission is properly sought will be treated accordingly. A redacted non-confidential version of the document must also be filed simultaneously with any confidential filing. All information, including confidential business information and documents for which confidential treatment is properly sought, submitted to the Commission for purposes of this Investigation may be disclosed to and used: (i) By the Commission, its employees and Offices, and contract personnel (a) for developing or maintaining the records of this or a related proceeding, or (b) in internal investigations, audits, reviews, and evaluations relating to the programs, personnel, and operations of the Commission including under 5 U.S.C. Appendix 3; or (ii) by U.S. government employees and contract personnel, solely for cybersecurity purposes. All contract personnel will sign appropriate nondisclosure agreements. All non-confidential written submissions will be available for public inspection at the Office of the Secretary and on EDIS.

The Commission vote for these determinations took place on September 8, 2020.

The authority for the Commission's determination is contained in section 337 of the Tariff Act of 1930, as amended (19 U.S.C. 1337), and in Part 210 of the Commission's Rules of Practice and Procedure (19 CFR part 210).

By order of the Commission.

Issued: September 8, 2020.

Lisa Barton,

Secretary to the Commission.

[FR Doc. 2020–20122 Filed 9–11–20; 8:45 am]

BILLING CODE 7020–02–P

DEPARTMENT OF JUSTICE

Drug Enforcement Administration

[Docket No. DEA–713]

Importer of Controlled Substances Application: Cerilliant Corporation

AGENCY: Drug Enforcement Administration, Justice.

ACTION: Notice of application.

SUMMARY: Cerilliant Corporation has applied to be registered as an importer of basic class(es) of controlled substance(s). Refer to Supplemental Information listed below for further drug information.

DATES: Registered bulk manufacturers of the affected basic class(es), and applicants therefore, may file written comments on or objections to the issuance of the proposed registration on or before October 14, 2020. Such persons may also file a written request for a hearing on the application on or before October 14, 2020.

ADDRESSES: Written comments should be sent to: Drug Enforcement Administration, Attention: DEA Federal Register Representative/DPW, 8701 Morrissette Drive, Springfield, Virginia 22152. All requests for a hearing must be sent to: Drug Enforcement Administration, Attn: Administrator, 8701 Morrissette Drive, Springfield, Virginia 22152. All request for a hearing should also be sent to: (1) Drug Enforcement Administration, Attn: Hearing Clerk/OALJ, 8701 Morrissette Drive, Springfield, Virginia 22152; and (2) Drug Enforcement Administration, Attn: DEA Federal Register Representative/DPW, 8701 Morrissette Drive, Springfield, Virginia 22152.

SUPPLEMENTARY INFORMATION: In accordance with 21 CFR 1301.34(a), this is notice that on July 23, 2020, Cerilliant Corporation, 811 Paloma Drive, Suite A, Round Rock, Texas 78665–2402, applied to be registered as an importer of the following basic classes of controlled substance(s):

Controlled substance	Drug code	Schedule
3-Fluoro-N-methylcathinone (3-FMC)	1233	I
Cathinone	1235	I
Methcathinone	1237	I
4-Fluoro-N-methylcathinone (4-FMC)	1238	I
Pentedrone (α-methylaminovalerophenone)	1246	I
Mephedrone (4-Methyl-N-methylcathinone)	1248	I
4-Methyl-N-ethylcathinone (4-MEC)	1249	I
Naphyrone	1258	I
N-Ethylamphetamine	1475	I
N,N-Dimethylamphetamine	1480	I
Fenethylline	1503	I
Methaqualone	2565	I
JWH-250 (1-Pentyl-3-(2-methoxyphenylacetyl) indole)	6250	I
SR-18 (Also known as RCS-8) (1-Cyclohexylethyl-3-(2-methoxyphenylacetyl) indole)	7008	I
5-Fluoro-UR-144 and XLR11 [1-(5-Fluoro-pentyl)1H-indol-3-yl] (2,2,3,3-tetramethylcyclopropyl)methanone	7011	I
AB-FUBINACA (N-(1-amino-3-methyl-1-oxobutan-2-yl)-1-(4-fluorobenzyl)-1H-indazole-3-carboxamide)	7012	I
JWH-019 (1-Hexyl-3-(1-naphthoyl)indole)	7019	I
AB-PINACA (N-(1-amino-3-methyl-1-oxobutan-2-yl)-1-pentyl-1H-indazole-3-carboxamide)	7023	I
THJ-2201 ([1-(5-fluoropentyl)-1H-indazol-3-yl](naphthalen-1-yl)methanone)	7024	I
AB-CHMINACA (N-(1-amino-3-methyl-1-oxobutan-2-yl)-1-(cyclohexylmethyl)-1H-indazole-3-carboxamide)	7031	I
ADB-PINACA (N-(1-amino-3,3-dimethyl-1-oxobutan-2-yl)-1-pentyl-1H-indazole-3-carboxamide)	7035	I
APINACA and AKB48 (N-(1-Adamantyl)-1-pentyl-1H-indazole-3-carboxamide)	7048	I
JWH-081 (1-Pentyl-3-(1-(4-methoxynaphthoyl) indole)	7081	I
SR-19 (Also known as RCS-4) (1-Pentyl-3-[(4-methoxy)-benzoyl] indole)	7104	I
JWH-018 (also known as AM678) (1-Pentyl-3-(1-naphthoyl)indole)	7118	I
JWH-122 (1-Pentyl-3-(4-methyl-1-naphthoyl) indole)	7122	I
UR-144 (1-Pentyl-1H-indol-3-yl)(2,2,3,3-tetramethylcyclopropyl)methanone	7144	I
JWH-073 (1-Butyl-3-(1-naphthoyl)indole)	7173	I
JWH-200 (1-[2-(4-Morpholinyl)ethyl]-3-(1-naphthoyl)indole)	7200	I
AM2201 (1-(5-Fluoropentyl)-3-(1-naphthoyl) indole)	7201	I
JWH-203 (1-Pentyl-3-(2-chlorophenylacetyl) indole)	7203	I
PB-22 (Quinolin-8-yl 1-pentyl-1H-indole-3-carboxylate)	7222	I
5F-PB-22 (Quinolin-8-yl 1-(5-fluoropentyl)-1H-indole-3-carboxylate)	7225	I
Alpha-ethyltryptamine	7249	I
Ibogaine	7260	I
CP-47,497 (5-(1,1-Dimethylheptyl)-2-[(1R,3S)-3-hydroxycyclohexyl-phenol)	7297	I
CP-47,497 C8 Homologue (5-(1,1-Dimethyloctyl)-2-[(1R,3S)3-hydroxycyclohexyl-phenol)	7298	I
Lysergic acid diethylamide	7315	I
2C-T-7 (2,5-Dimethoxy-4-(n)-propylthiophenethylamine	7348	I
Marihuana	7360	I
Parahexyl	7374	I
Mescaline	7381	I
2C-T-2 (2-(4-Ethylthio-2,5-dimethoxyphenyl) ethanamine)	7385	I
3,4,5-Trimethoxyamphetamine	7390	I

Controlled substance	Drug code	Schedule
4-Bromo-2,5-dimethoxyamphetamine	7391	I
4-Bromo-2,5-dimethoxyphenethylamine	7392	I
4-Methyl-2,5-dimethoxyamphetamine	7395	I
2,5-Dimethoxyamphetamine	7396	I
JWH-398 (1-Pentyl-3-(4-chloro-1-naphthoyl) indole)	7398	I
3,4-Methylenedioxyamphetamine	7400	I
5-Methoxy-3,4-methylenedioxyamphetamine	7401	I
N-Hydroxy-3,4-methylenedioxyamphetamine	7402	I
3,4-Methylenedioxy-N-ethylamphetamine	7404	I
3,4-Methylenedioxymethamphetamine	7405	I
4-Methoxyamphetamine	7411	I
5-Methoxy-N-N-dimethyltryptamine	7431	I
Alpha-methyltryptamine	7432	I
Bufotenine	7433	I
Diethyltryptamine	7434	I
Dimethyltryptamine	7435	I
Psilocybin	7437	I
Psilocyn	7438	I
5-Methoxy-N,N-diisopropyltryptamine	7439	I
N-Ethyl-1-phenylcyclohexylamine	7455	I
1-(1-Phenylcyclohexyl)pyrrolidine	7458	I
1-[1-(2-Thienyl)cyclohexyl]piperidine	7470	I
N-Benzylpiperazine	7493	I
4-MePPP (4-Methyl-alphapyrrolidinopropiophenone)	7498	I
2C-D (2-(2,5-Dimethoxy-4-methylphenyl) ethanamine)	7508	I
2C-E (2-(2,5-Dimethoxy-4-ethylphenyl) ethanamine)	7509	I
2C-H 2-(2,5-Dimethoxyphenyl) ethanamine)	7517	I
2C-I 2-(4-iodo-2,5-dimethoxyphenyl) ethanamine)	7518	I
2C-C 2-(4-Chloro-2,5-dimethoxyphenyl) ethanamine)	7519	I
2C-N (2-(2,5-Dimethoxy-4-nitro-phenyl) ethanamine)	7521	I
2C-P (2-(2,5-Dimethoxy-4-(n)-propylphenyl) ethanamine)	7524	I
2C-T-4 (2-(4-Isopropylthio)-2,5-dimethoxyphenyl) ethanamine)	7532	I
MDPV (3,4-Methylenedioxypyrovalerone)	7535	I
25B-NBOMe (2-(4-bromo-2,5-dimethoxyphenyl)-N-(2-methoxybenzyl) ethanamine)	7536	I
25C-NBOMe (2-(4-chloro-2,5-dimethoxyphenyl)-N-(2-methoxybenzyl) ethanamine)	7537	I
25I-NBOMe (2-(4-iodo-2,5-dimethoxyphenyl)-N-(2-methoxybenzyl) ethanamine)	7538	I
Methylone (3,4-Methylenedioxy-N-methylcathinone)	7540	I
Butylone	7541	I
Pentylone	7542	I
alpha-pyrrolidinopentiophenone (α-PVP)	7545	I
alpha-pyrrolidinobutiophenone (α-PBP)	7546	I
AM-694 (1-(5-Fluoropentyl)-3-(2-iodobenzoyl) indole)	7694	I
Desomorphine	9055	I
Etorphine (except HCl)	9056	I
Codeine methylbromide	9070	I
Heroin	9200	I
Morphine-N-oxide	9307	I
Normorphine	9313	I
Pholcodine	9314	I
U-47700 (3,4-dichloro-N-[2-(dimethylamino)cyclohexyl]-N-methylbenzamide)	9547	I
AH-7921 (3,4-dichloro-N-[(1-dimethylamino)cyclohexylmethyl]benzamide))	9551	I
Acetylmethadol	9601	I
Allylprodine	9602	I
Alphacetylmethadol except levo-alphacetylmethadol	9603	I
Alphameprodine	9604	I
Alphamethadol	9605	I
Betacetylmethadol	9607	I
Betameprodine	9608	I
Betamethadol	9609	I
Betaprodine	9611	I
Dextromoramide	9613	I
Dipipanone	9622	I
Hydroxypethidine	9627	I
Noracymethadol	9633	I
Norlevorphanol	9634	I
Normethadone	9635	I
Racemoramide	9645	I
Trimeperidine	9646	I
1-Methyl-4-phenyl-4-propionoxypiperidine	9661	I
Tilidine	9750	I
Para-Fluorofentanyl	9812	I
3-Methylfentanyl	9813	I
Alpha-methylfentanyl	9814	I
Acetyl-alpha-methylfentanyl	9815	I

Controlled substance	Drug code	Schedule
Beta-hydroxyfentanyl	9830	I
Beta-hydroxy-3-methylfentanyl	9831	I
Alpha-methylthiofentanyl	9832	I
3-Methylthiofentanyl	9833	I
Thiofentanyl	9835	I
Fentanyl related-substances as defined in 21 CFR 1308.11(h)	9850	I
Methamphetamine	1105	II
Methylphenidate	1724	II
Amobarbital	2125	II
Pentobarbital	2270	II
Secobarbital	2315	II
Glutethimide	2550	II
Nabilone	7379	II
1-Phenylcyclohexylamine	7460	II
Phencyclidine	7471	II
Phenylacetone	8501	II
1-Piperidinocyclohexanecarbonitrile	8603	II
Alphaprodine	9010	II
Dihydrocodeine	9120	II
Ecgonine	9180	II
Ethylmorphine	9190	II
Levomethorphan	9210	II
Levorphanol	9220	II
Meperidine	9230	II
Dextropropoxyphene, bulk (non-dosage forms)	9273	II
Levo-alphacetylmethadol	9648	II
Noroxymorphone	9668	II
Racemethorphan	9732	II
Alfentanil	9737	II
Remifentanil	9739	II
Sufentanil	9740	II
Carfentanil	9743	II
Tapentadol	9780	II

The company plans to import the listed controlled substances for the manufacturing of analytical reference standards and distribution to their research and forensic customers. Approval of permit application will occur only when the registrant's activity is consistent with what is authorized under 21 U.S.C. 952(a)(2). Authorization will not extend to the import of Food and Drug Administration-approved or non-approved finished dosage forms for commercial sale.

William T. McDermott,

Assistant Administrator.

[FR Doc. 2020–20159 Filed 9–11–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF JUSTICE

Drug Enforcement Administration

[Docket No. DEA–712]

Bulk Manufacturer of Controlled Substances Application: Organix Inc.

AGENCY: Drug Enforcement Administration, Justice.

ACTION: Notice of application.

SUMMARY: Organix Inc. has applied to be registered as a bulk manufacturer of basic class(es) of controlled substance(s). Refer to Supplemental Information listed below for further drug information.

DATES: Registered bulk manufacturers of the affected basic class(es), and applicants therefore, may file written comments on or objections to the issuance of the proposed registration on or before November 13, 2020 Such persons may also file a written request for a hearing on the application on or before November 13, 2020.

ADDRESSES: Written comments should be sent to: Drug Enforcement Administration, Attention: DEA Federal Register Representative/DPW, 8701 Morrissette Drive, Springfield, Virginia 22152.

SUPPLEMENTARY INFORMATION: In accordance with 21 CFR 1301.33(a), this is notice that on August 5, 2020, Organix Inc., 240 Salem Street, Woburn, Massachusetts 01801–2029, applied to be registered as a bulk manufacturer of the following basic class(es) of a controlled substance(s):

Controlled substance	Drug code	Schedule
5-Methoxy-N-N-dimethyltryptamine.	7431	I

The company plans to synthesize the above-listed controlled substance for distribution to its customers. No other activity for this drug code is authorized for this registration.

William T. McDermott,

Assistant Administrator.

[FR Doc. 2020–20162 Filed 9–11–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF JUSTICE

Drug Enforcement Administration

[Docket No. DEA–709]

Bulk Manufacturer of Controlled Substances Application: Cambridge Isotype Lab

AGENCY: Drug Enforcement Administration, Justice.

ACTION: Notice of application.

SUMMARY: Cambridge Isotype Lab has applied to be registered as a bulk manufacturer of basic class(es) of controlled substance(s). Refer to Supplemental Information listed below for further drug(s) information.

DATES: Registered bulk manufacturers of the affected basic class(es), and applicants therefore, may file written comments on or objections to the issuance of the proposed registration on or before November 13, 2020. Such persons may also file a written request for a hearing on the application on or before November 13, 2020.

ADDRESSES: Written comments should be sent to: Drug Enforcement Administration, Attention: DEA Federal Register Representative/DPW, 8701 Morrissette Drive, Springfield, Virginia 22152.

SUPPLEMENTARY INFORMATION: In accordance with 21 CFR 1301.33(a), this is notice that on July 23, 2020, Cambridge Isotype Lab 50 Frontage Road, Andover, Massachusetts 01810–5413, applied to be registered as an bulk manufacturer of the following basic class(es) of controlled substance(s):

Controlled substance	Drug code	Schedule
Tetrahydrocannabinols ...	7370	I

The company plans to synthetically bulk manufacture the controlled substance Tetrahydrocannabinols to produce analytical standards for distribution to its customers. No other activity for this drug code is authorized for this registration.

William T. McDermott,

Assistant Administrator.

[FR Doc. 2020–20160 Filed 9–11–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF JUSTICE

Drug Enforcement Administration

[Docket No. DEA–711]

Importer of Controlled Substances Application: Novitium Pharma LLC

AGENCY: Drug Enforcement Administration, Justice.

ACTION: Notice of application.

SUMMARY: Novitium Pharma LLC has applied to be registered as an importer of basic class(es) of controlled substance(s). Refer to Supplemental Information listed below for further drug(s) information.

DATES: Registered bulk manufacturers of the affected basic class(es), and applicants therefore, may file written comments on or objections to the issuance of the proposed registration on or before October 14, 2020. Such persons may also file a written request for a hearing on the application on or before October 14, 2020.

ADDRESSES: Written comments should be sent to: Drug Enforcement Administration, Attention: DEA Federal Register Representative/DPW, 8701 Morrissette Drive, Springfield, Virginia 22152. All requests for a hearing must be sent to: Drug Enforcement Administration, Attn: Administrator, 8701 Morrissette Drive, Springfield, Virginia 22152. All requests for a hearing should also be sent to: (1) Drug Enforcement Administration, Attn: Hearing Clerk/OALJ, 8701 Morrissette Drive, Springfield, Virginia 22152; and (2) Drug Enforcement Administration, Attn: DEA Federal Register Representative/DPW, 8701 Morrissette Drive, Springfield, Virginia 22152.

SUPPLEMENTARY INFORMATION: In accordance with 21 CFR 1301.34(a), this is notice that on August 18, 2020, Novitium Pharma LLC, 70 Lake Drive, East Windsor, New Jersey 08520, applied to be registered as an importer of the following basic class(es) of controlled substance(s):

Controlled substance	Drug code	Schedule
Lisdexamfetamine ...	1205	II
Levorphanol	9220	II

The company plans to import the listed controlled substance Lisdexamfetamine as a raw Active Pharmaceutical Ingredients (API) material for drug product development and research purposes only. The company may import Lisdexamfetamine API for research purposes only but not for the manufacturing of Food and Drug Administration (FDA)-approved products.

The company plans to import the listed controlled substance Levorphanol to develop the manufacturing process for a drug product that will in turn be used to produce a tablet equivalent to the current brand product.

Approval of permit applications will occur only when the registrant's business activity is consistent with what is authorized under 21 U.S.C. 952(a)(2). Authorization will not extend to the import of FDA-approved or non-approved finished dosage forms for commercial sale.

William T. McDermott,

Assistant Administrator.

[FR Doc. 2020–20161 Filed 9–11–20; 8:45 am]

BILLING CODE P

DEPARTMENT OF LABOR

Employment and Training Administration

Notice of a Change in Status of the Extended Benefit (EB) Program for Nevada

AGENCY: Employment and Training Administration, Labor.

ACTION: Notice.

This notice announces a retroactive change in benefit period eligibility under the EB program for Nevada.

The following change has occurred since the publication of the last notice regarding the State's EB status:

Based on Nevada's State law, which provides for the temporary adoption of the optional TUR trigger during periods of 100 percent Federal financing, and data released by the Bureau of Labor Statistics on May 22, 2020, the seasonally-adjusted total unemployment rate for Nevada rose to meet the 8.0 percent threshold to trigger ''on'' to a high unemployment period in EB. The payable period for Nevada under the high unemployment period is retroactive to June 7, 2020, and eligibility for claimants has been extended from a potential duration of up to 13 weeks to a potential duration of up to 20 weeks in the EB program.

The trigger notice covering state eligibility for the EB program can be found at: *http://ows.doleta.gov/unemploy/claims_arch.as*

Information for Claimants

The duration of benefits payable in the EB program, and the terms and conditions on which they are payable, are governed by the Federal-State Extended Unemployment Compensation Act of 1970, as amended, and the operating instructions issued to the states by the U.S. Department of Labor. In the case of a state beginning an EB period, the State Workforce Agency will furnish a written notice of potential entitlement to each individual who has exhausted all rights to regular benefits and is potentially eligible for EB (20 CFR 615.13(c)(1)).

Persons who believe they may be entitled to EB, or who wish to inquire about their rights under the program, should contact their State Workforce Agency.

FOR FURTHER INFORMATION CONTACT: U.S. Department of Labor, Employment and Training Administration, Office of Unemployment Insurance Room S–4524, Attn: Thomas Stengle, 200 Constitution Avenue NW, Washington, DC 20210, telephone number (202)–693–2991 (this is not a toll-free number) or by email: *Stengle.Thomas@dol.gov.*

Signed in Washington, DC.

John Pallasch,

Assistant Secretary for Employment and Training.

[FR Doc. 2020–20192 Filed 9–11–20; 8:45 am]

BILLING CODE 4510–FW–P

DEPARTMENT OF LABOR

Office of Federal Contract Compliance Programs

Affirmative Action Program Verification Interface; New Information Collection Requirements; Comment Request

AGENCY: Office of Federal Contract Compliance Programs, Labor.

ACTION: Notice.

SUMMARY: The Department of Labor (DOL), as part of its continuing effort to reduce paperwork and respondent burden, conducts a pre-clearance consultation program to provide the general public and federal agencies with an opportunity to comment on proposed and/or continuing collections of information in accordance with the Paperwork Reduction Act of 1995 (PRA). The program helps to ensure that requested data can be provided in the desired format, reporting burden (time and financial resources) is minimized, collection instruments are clearly understood, and the impact of collection requirements on respondents can be properly assessed. Currently, the Office of Federal Contract Compliance Programs (OFCCP) is soliciting comments concerning its proposal to obtain approval from the Office of Management and Budget (OMB) to implement the Affirmative Action Program Verification Interface (AAP–VI). A copy of the proposed information collection request can be obtained by contacting the office listed below in the **FOR FURTHER INFORMATION CONTACT** section of this Notice or by accessing it at *https://www.regulations.gov/.*

DATES: Written comments must be submitted to the office listed in the addresses section below on or before November 13, 2020.

ADDRESSES: You may submit comments by any of the following methods:

Electronic comments: The federal e-Rulemaking portal at *https://www.regulations.gov/.* Follow the instructions found on that website for submitting comments.

Mail, Hand Delivery, Courier: Addressed to Tina Williams, Director, Division of Policy and Program Development, Office of Federal Contract Compliance Programs, 200 Constitution Avenue NW, Room C–3325, Washington, DC 20210.

Instructions: Please submit one copy of your comments by only one method. For faster submission, we encourage commenters to transmit their comment electronically via the *https://www.regulations.gov/* website. Comments that are mailed to the address provided above must be postmarked before the close of the comment period. All submissions must include OFCCP's name for identification. Comments submitted in response to the notice, including any personal information provided, become a matter of public record and will be posted on *https://www.regulations.gov/.* Comments will also be summarized and/or included in the request for OMB approval of the information collection request.

FOR FURTHER INFORMATION CONTACT: Tina Williams, Director, Division of Policy and Program Development, Office of Federal Contract Compliance Programs, Room C–3325, 200 Constitution Avenue NW, Washington, DC 20210. Telephone: (202) 693–0103 (voice) or (202) 693–1337 (TTY) (these are not toll-free numbers). Copies of this notice may be obtained in alternative formats (large print, braille, audio recording) upon request by calling the numbers listed above.

SUPPLEMENTARY INFORMATION:

I. Background: OFCCP administers and enforces the three equal employment opportunity laws listed below.

- Executive Order 11246, as amended (E.O. 11246)
- Section 503 of the Rehabilitation Act of 1973, as amended (Section 503)
- Vietnam Era Veterans' Readjustment Assistance Act of 1974, as amended (VEVRAA)

These authorities prohibit employment discrimination by covered federal contractors and subcontractors and require that they provide equal employment opportunities regardless of race, color, religion, sex, sexual orientation, gender identity, national origin, disability, or status as a protected veteran. Additionally, federal contractors and subcontractors are prohibited from discriminating against applicants and employees for inquiring about, discussing, or disclosing information about their pay or the pay of their co-workers, subject to certain limitations. E.O. 11246's basic coverage applies to federal contractors and subcontractors and to federally assisted construction contractors holding a government contract in excess of $10,000, or government contracts that have, or can reasonably be expected to have, an aggregate total value exceeding $10,000 in a 12-month period. E.O. 11246 also applies to government bills of lading, depositories of federal funds in any amount, and to financial institutions that are issuing and paying agents for U.S. Savings Bonds. E.O. 11246's Affirmative Action Program (AAP) requirements apply to federal contractors and subcontractors with 50 or more employees and a contract of $50,000 or more. Section 503 prohibits employment discrimination against applicants and employees because of physical or mental disability and requires affirmative action to ensure that persons are treated without regard to disability. Section 503 applies to federal contractors and subcontractors with contracts in excess of $15,000, and its AAP coverage applies to federal contractors and subcontractors with 50 or more employees and a contract of $50,000 or more. VEVRAA prohibits employment discrimination against protected veterans and requires affirmative action to ensure that persons are treated without regard to their status as a protected veteran. VEVRAA applies to federal contractors and subcontractors with contracts of $150,000 or more, and its AAP coverage applies to federal contractors and subcontractors with 50 or more employees and a contract of $150,000 or more. This information collection request (ICR) seeks authorization for an annual Affirmative Action Program online certification process for federal contractors and for a secure method for federal contractors to submit AAPs electronically to OFCCP when they are scheduled for a compliance evaluation.

II. Review Focus: OFCCP is particularly interested in comments which:

- Evaluate the proposed frequency and level of information collection;
- Evaluate whether the proposed collection of information is necessary for the enforcement and compliance assistance functions of the agency that support the agency's compliance mission, including whether the information will have practical utility;
- 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;
- Enhance the quality, utility, and clarity of the information to be collected; and
- 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.

III. Current Actions: OFCCP seeks approval of this new information collection in order to carry out its responsibilities to enforce the nondiscrimination and affirmative action provisions of the three legal authorities it administers.

Type of Review: New Collection.

Agency: Office of Federal Contract Compliance Programs.

Title: Affirmative Action Program Verification Interface.

OMB Control Number: 1250–[NEW].

Agency Number: None.

Affected Public: Business or other for-profit entities.

Total Respondents: 116,898.

Total Annual Respondents: 116,898.

Average Time per Response: 0.3 hours for account creation. 0.2 hours for AAP Submission. 0.1 hours for SAM Cert Question.

Estimated Total Burden Hours: 47,759 in the first year. 13,041 in subsequent years.

Frequency: Annual.

Total Other Burden Costs: $0.

Signed in Washington, DC, this September 8, 2020.

Harvey D. Fort,

Deputy Director, Division of Policy and Program Development, Office of Federal Contract Compliance Programs.

[FR Doc. 2020–20105 Filed 9–11–20; 8:45 am]

BILLING CODE 4510–CM–P

DEPARTMENT OF LABOR

Mine Safety and Health Administration

[OMB Control No. 1219–0133]

Proposed Extension of Information Collection; Hazard Communication—30 CFR Part 47

AGENCY: Mine Safety and Health Administration, Labor.

ACTION: Request for public comments.

SUMMARY: The Department of Labor, as part of its continuing effort to reduce paperwork and respondent burden, conducts a pre-clearance consultation program to provide the general public and Federal agencies with an opportunity to comment on proposed collections of information in accordance with the Paperwork Reduction Act of 1995. This program helps to ensure that requested data can be provided in the desired format, reporting burden (time and financial resources) is minimized, collection instruments are clearly understood, and the impact of collection requirements on respondents can be properly assessed. Currently, the Mine Safety and Health Administration (MSHA) is soliciting comments on the information collection for Hazard Communication—30 CFR part 47.

DATES: All comments must be received on or before November 13, 2020.

ADDRESSES: You may submit comment as follows. Please note that late, untimely filed comments will not be considered.

Electronic Submissions: Submit electronic comments in the following way:

• *Federal eRulemaking Portal: https://www.regulations.gov.* Follow the instructions for submitting comments for docket number MSHA–2020–0026. Comments submitted electronically, including attachments, to *https://www.regulations.gov* will be posted to the docket, with no changes. Because your comment will be made public, you are 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 your or anyone else's Social Security number or confidential business information.

• 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.

Written/Paper Submissions: Submit written/paper submissions in the following way:

• *Mail/Hand Delivery:* Mail or visit DOL–MSHA, Office of Standards, Regulations, and Variances, 201 12th Street South, Suite 4E401, Arlington, VA 22202–5452.

• MSHA will post your comment as well as any attachments, except for information submitted and marked as confidential, in the docket at *https://www.regulations.gov.*

FOR FURTHER INFORMATION CONTACT: Roslyn Fontaine, Deputy Director, Office of Standards, Regulations, and Variances, MSHA, at *MSHA.information.collections@dol.gov* (email); (202) 693–9440 (voice); or (202) 693–9441 (facsimile).

SUPPLEMENTARY INFORMATION:

I. Background

Section 103(h) of the Federal Mine Safety and Health Act of 1977 (Mine Act), 30 U.S.C. 813(h), authorizes MSHA to collect information necessary to carry out its duty in protecting the safety and health of miners. Further, section 101(a) of the Mine Act, 30 U.S.C. 811(a), authorizes the Secretary of Labor to develop, promulgate, and revise as may be appropriate, improved mandatory health or safety standards for the protection of life and prevention of injuries in coal or other mines.

Section 101(a)(7) of the Mine Act, 30 U.S.C. 811(a)(7), requires, in part, that mandatory standards prescribe the use of labels or other appropriate forms of warning as are necessary to ensure that miners are apprised of all hazards to which they are exposed, relevant symptoms and appropriate emergency treatment, and proper conditions and precautions for safe use or exposure.

MSHA's hazardous communications standards in 30 CFR part 47 require mine operators to evaluate the hazards of chemicals they produce or use and to provide information to miners concerning chemical hazards by means of a written hazard communication program including a list of all hazardous chemicals known at the mine, labeling containers of hazardous chemicals, providing access to Material Safety Data Sheets, and administering initial miner training.

II. Desired Focus of Comments

MSHA is soliciting comments concerning the proposed information collection related to Hazard Communication—30 CFR part 47. MSHA is particularly interested in comments that:

• Evaluate whether the collection of information is necessary for the proper performance of the functions of the Agency, including whether the information has practical utility;

• Evaluate the accuracy of MSHA's estimate of the burden of the collection of information, including the validity of the methodology and assumptions used;

• Suggest methods to enhance the quality, utility, and clarity of the information to be collected; and

• 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.

Background documents related to this information collection request are available at *https://regulations.gov* and in DOL–MSHA located at 201 12th Street South, Suite 4E401, Arlington, VA 22202–5452. Questions about the information collection requirements may be directed to the person listed in the **FOR FURTHER INFORMATION** section of this notice from the previous collection of information.

III. Current Actions

This information collection request concerns provisions for Hazard Communication—30 CFR part 47. MSHA has updated the data with respect to the number of respondents, responses, burden hours, and burden costs supporting this information collection request from the previous information collection request.

Type of Review: Extension, without change, of a currently approved collection.

Agency: Mine Safety and Health Administration.

OMB Number: 1219–0133.

Affected Public: Business or other for-profit.

Number of Respondents: 15,584.

Frequency: On occasion.

Number of Responses: 907,409.

Annual Burden Hours: 148,236 hours.

Annual Respondent or Recordkeeper Cost: $9,175.

Comments submitted in response to this notice will be summarized in the request for Office of Management and Budget approval of the proposed information collection request; they will become a matter of public record and will be available at *https://www.reginfo.gov.*

Roslyn B. Fontaine,

Certifying Officer.

[FR Doc. 2020–20194 Filed 9–11–20; 8:45 am]

BILLING CODE 4510–43–P

DEPARTMENT OF LABOR

Mine Safety and Health Administration

[OMB Control No. 1219–0007]

Proposed Extension of Information Collection; Mine Accident, Injury, and Illness Report and Quarterly Mine Employment and Coal Production Report

AGENCY: Mine Safety and Health Administration, Labor.

ACTION: Request for public comments.

SUMMARY: The Department of Labor, as part of its continuing effort to reduce paperwork and respondent burden, conducts a pre-clearance consultation program to provide the general public and Federal agencies with an opportunity to comment on proposed collections of information in accordance with the Paperwork Reduction Act of 1995. This program helps to ensure that requested data can be provided in the desired format, reporting burden (time and financial resources) is minimized, collection instruments are clearly understood, and the impact of collection requirements on respondents can be properly assessed. Currently, the Mine Safety and Health Administration (MSHA) is soliciting comments on the information collection for Mine Accident, Injury, and Illness Report and Quarterly Mine Employment and Coal Production Report.

DATES: All comments must be received on or before November 13, 2020.

ADDRESSES: You may submit comment as follows. Please note that late, untimely filed comments will not be considered.

Electronic Submissions: Submit electronic comments in the following way:

- *Federal eRulemaking Portal: https://www.regulations.gov.* Follow the instructions for submitting comments for docket number MSHA–2020–0025. Comments submitted electronically, including attachments, to *https://www.regulations.gov* will be posted to the docket, with no changes. Because your comment will be made public, you are 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 your or anyone else's Social Security number or confidential business information.
- 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.

Written/Paper Submissions: Submit written/paper submissions in the following way:

- *Mail/Hand Delivery:* Mail or visit DOL–MSHA, Office of Standards, Regulations, and Variances, 201 12th Street South, Suite 4E401, Arlington, VA 22202–5452.
- MSHA will post your comment as well as any attachments, except for information submitted and marked as confidential, in the docket at *https://www.regulations.gov.*

FOR FURTHER INFORMATION CONTACT: Roslyn Fontaine, Deputy Director, Office of Standards, Regulations, and Variances, MSHA, at *MSHA.information.collections@dol.gov* (email); (202) 693–9440 (voice); or (202) 693–9441 (facsimile).

SUPPLEMENTARY INFORMATION:

I. Background

Section 103(h) of the Federal Mine Safety and Health Act of 1977 (Mine Act), 30 U.S.C. 813(h), authorizes MSHA to collect information necessary to carry out its duty in protecting the safety and health of miners. Further, section 101(a) of the Mine Act, 30 U.S.C. 811, authorizes the Secretary of Labor (Secretary) to develop, promulgate, and revise as may be appropriate, improved mandatory health or safety standards for the protection of life and prevention of injuries in coal or other mines.

The reporting and recordkeeping provisions in 30 CFR part 50 (Part 50), Notification, Investigation, Reports and Records of Accidents, Injuries and Illnesses, Employment and Coal Production in Mines, are essential elements in MSHA's statutory mandate to reduce work-related injuries and illnesses among the nation's miners (30 U.S.C. 801).

Section 50.10 requires mine operators and independent contractors to immediately notify MSHA in the event of an accident. This immediate notification is critical to MSHA's timely investigation and assessment of the cause of the accident.

Section 50.11 requires that the mine operator or independent contractor investigate each accident and occupational injury and prepare a report. The mine operator or independent contractor may not use MSHA Form 7000–1 as the investigation report, except if the operator or contractor employs fewer than 20 miners and the injury is not related to an accident.

Section 50.20 requires mine operators and independent contractors to report each accident, injury, and illness to MSHA on Form 7000–1 within 10 working days after an accident or injury has occurred or an occupational illness has been diagnosed. The use of MSHA Form 7000–1 provides for uniform information gathering across the mining industry.

Section 50.30 requires that all mine operators and independent contractors working on mine property report employment to MSHA quarterly on Form 7000–2, and that coal mine operators and independent contractors also report coal production.

Accident, injury, and illness data, when correlated with employment and production data, provide information that MSHA uses to improve its safety and health enforcement programs, focus its education and training efforts, and establish priorities for its technical assistance activities in mine safety and health. Maintaining a current database allows MSHA to identify and direct increased attention to those mines, industry segments, and geographical areas where hazardous trends are developing. This could not be done effectively using historical data. The information collected under Part 50 is the most comprehensive and reliable occupational data available concerning the mining industry.

Section 103(d) of the Mine Act mandates that each accident be investigated by the operator to determine the cause and means of preventing a recurrence. Operators must keep records of such accidents and investigations and make them available to the Secretary or the Secretary's authorized representative and the appropriate State agency.

Section 103(h) requires operators to keep any records and make any reports that are reasonably necessary for MSHA to perform its duties under the Mine Act. Section 103(j) requires operators to notify MSHA of the occurrence of an accident and to take appropriate measures to preserve any evidence that would assist in the investigation into the causes of the accident.

II. Desired Focus of Comments

MSHA is soliciting comments concerning the proposed information collection related to Mine Accident, Injury, and Illness Report and Quarterly Mine Employment and Coal Production Report. MSHA is particularly interested in comments that:

• Evaluate whether the collection of information is necessary for the proper performance of the functions of the Agency, including whether the information has practical utility;

• Evaluate the accuracy of MSHA's estimate of the burden of the collection of information, including the validity of the methodology and assumptions used;

• Suggest methods to enhance the quality, utility, and clarity of the information to be collected; and

• 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.

Background documents related to this information collection request are available at *https://regulations.gov* and in DOL–MSHA located at 201 12th Street South, Suite 4E401, Arlington, VA 22202–5452. Questions about the information collection requirements may be directed to the person listed in the **FOR FURTHER INFORMATION** section of this notice from the previous collection of information.

III. Current Actions

This information collection request concerns provisions for Mine Accident, Injury, and Illness Report and Quarterly Mine Employment and Coal Production Report. MSHA has updated the data with respect to the number of respondents, responses, burden hours, and burden costs supporting this information collection request from the previous information collection request.

Type of Review: Extension, without change, of a currently approved collection.

Agency: Mine Safety and Health Administration.

OMB Number: 1219–0007.

Affected Public: Business or other for-profit.

Number of Respondents: 25,067.

Frequency: On occasion.

Number of Responses: 112,414.

Annual Burden Hours: 131,632 hours.

Annual Respondent or Recordkeeper Cost: $2,946.

MSHA Forms: MSHA Form 7000–1, Mine Accident, Injury, and Illness Report; MSHA Form 7000–2, Quarterly Mine Employment and Coal Production Report.

Comments submitted in response to this notice will be summarized in the request for Office of Management and Budget approval of the proposed information collection request; they will become a matter of public record and will be available at *https://www.reginfo.gov.*

Roslyn B. Fontaine,

Certifying Officer.

[FR Doc. 2020–20193 Filed 9–11–20; 8:45 am]

BILLING CODE 4510–43–P

NATIONAL AERONAUTICS AND SPACE ADMINISTRATION

[20–071]

Name of Information Collection: Information Collection; Improving Customer Experience (OMB Circular A–11, Section 280 Implementation)

AGENCY: National Aeronautics and Space Administration.

ACTION: Notice; request for comment.

SUMMARY: The National Aeronautics and Space Administration (NASA) has under OMB review the following proposed Information Collection Request ''Improving Customer Experience (OMB Circular A–11, Section 280 Implementation)'' for approval under the Paperwork Reduction Act (PRA).

DATES: Comments are due by 10/03/2020.

ADDRESSES: Submit comments identified by Information Collection, Improving Customer Experience (OMB Circular A–11, Section 280 Implementation), by any of the following methods:

• *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.

• *Mail:* R. Travis Kantz, NASA Clearance Officer, NASA Headquarters, 300 E Street SW, Washington, DC 20546, Mail Code: JSC/HQ–IB–20, 281–792–7885 or email *Travis.Kantz@nasa.gov.*

Instructions: Please submit comments only and cite Information Collection, ''Improving Customer Experience (OMB Circular A–11, Section 280 Implementation)'' in all correspondence related to this collection. To confirm receipt of your comment(s), please check *regulations.gov,* approximately two-to-three business days after submission to verify posting (except allow 30 days for posting of comments submitted by mail).

FOR FURTHER INFORMATION CONTACT: Requests for additional information or copies of the information collection instrument(s) and instructions should be directed to Roger Kantz, NASA Clearance Officer, NASA Headquarters, 300 E Street SW, JF0000, Washington, DC 20546 or email *Roger.T.Kantz@nasa.gov.*

SUPPLEMENTARY INFORMATION:

I. Abstract:

A modern, streamlined and responsive customer experience means: Raising government-wide customer experience to the average of the private sector service industry; developing indicators for high-impact Federal programs to monitor progress towards excellent customer experience and mature digital services; and providing the structure (including increasing transparency) and resources to ensure customer experience is a focal point for agency leadership.

This proposed information collection activity provides a means to garner customer and stakeholder feedback in an efficient, timely manner in accordance with the Administration's commitment to improving customer service delivery as discussed in Section 280 of OMB Circular A–11 at *https://www.performance.gov/cx/a11-280.pdf.*

As discussed in OMB guidance, agencies should identify their highest-impact customer journeys (using customer volume, annual program cost, and/or knowledge of customer priority as weighting factors) and select touchpoints/transactions within those journeys to collect feedback.

These results will be used to improve the delivery of Federal services and programs. It will also provide government-wide data on customer experience that can be displayed on *www.performance.gov* to help build transparency and accountability of

Federal programs to the customers they serve.

As a general matter, these information collections will not result in any new system of records containing privacy information and will not ask questions of a sensitive nature, such as sexual behavior and attitudes, religious beliefs, and other matters that are commonly considered private.

NASA will only submit collections if they meet the following criteria.

- The collections are voluntary;
- The collections are low-burden for respondents (based on considerations of total burden hours or burden-hours per respondent) and are low-cost for both the respondents and the Federal Government;
- The collections are non-controversial and do not raise issues of concern to other Federal agencies;
- Any collection is targeted to the solicitation of opinions from respondents who have experience with the program or may have experience with the program in the near future;
- Personally identifiable information (PII) is collected only to the extent necessary and is not retained;
- Information gathered is intended to be used for general service improvement and program management purposes;
- Upon agreement between OMB and the agency all or a subset of information may be released as part of A–11, Section 280 requirements only on *performance.gov.* Summaries of customer research and user testing activities may be included in public-facing customer journey maps or summaries.
- Additional release of data must be done coordinated with OMB.

These collections will allow for ongoing, collaborative and actionable communications between the Agency, its customers and stakeholders, and OMB as it monitors agency compliance on Section 280. These responses will inform efforts to improve or maintain the quality of service offered to the public. If this information is not collected, vital feedback from customers and stakeholders on services will be unavailable.

II. Methods of Collection

Electronic and optionally by paper.

III. Data

Title: Improving Customer Experience (OMB Circular A–11, Section 280 Implementation).

Current Action: New Collection of Information.

Type of Review: New.

Affected Public: Individuals and Households, Businesses and Organizations, State, Local or Tribal Government.

Estimated Number of Respondents: Below is a preliminary estimate of the aggregate burden hours for this new collection. NASA will provide refined estimates of burden in subsequent notices.

Estimated Annual Number of Activities: 5.

Average Number of Respondents per Activity: 1.

Annual Responses: 2,001,550.

Estimated Time per Response: 2 minutes–60 minutes, dependent upon activity.

Burden Hours: 101,125 burden hours.

IV. Request for Comments

Comments submitted in response to this notice will be summarized and/or included in the request for OMB approval. Comments are invited on: (a) Whether the collection of information is necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility; (b) the accuracy of the agency's estimate of the burden of the collection of information; (c) ways to enhance the quality, utility, and clarity of the information to be collected; (d) ways to minimize the burden of the collection of information on respondents, including through the use of automated collection techniques or other forms of information technology; and (e) estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

Burden means the total time, effort, or financial resources expended by persons to generate, maintain, retain, disclose or provide information to or for a Federal agency. This includes the time needed to review instructions; to develop, acquire, install and utilize technology and systems for the purpose of collecting, validating and verifying information, processing and maintaining information, and disclosing and providing information; to train personnel and to be able to respond to a collection of information, to search data sources, to complete and review the collection of information; and to transmit or otherwise disclose the information.

All written comments will be available for public inspection *Regulations.gov.*

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 Office of Management and Budget control number.

Roger Kantz,

NASA PRA Clearance Officer.

[FR Doc. 2020–20108 Filed 9–11–20; 8:45 am]

BILLING CODE 7510–13–P

NATIONAL FOUNDATION ON THE ARTS AND THE HUMANITIES

Institute of Museum and Library Services

Notice of Proposed Information Collection Request: Generic Clearance for the Collection of Qualitative Feedback on Agency Service Delivery

AGENCY: Institute of Museum and Library Services, National Foundation on the Arts and the Humanities.

ACTION: Notice, request for comments, collection of information.

SUMMARY: The Institute of Museum and Library Services (IMLS), as part of its continuing effort to reduce paperwork and respondent burden, conducts a pre-clearance consultation program to provide the general public and federal agencies with an opportunity to comment on proposed and/or continuing collections of information in accordance with the Paperwork Reduction Act. This pre-clearance consultation program helps to ensure that requested data can be provided in the desired format, reporting burden (time and financial resources) is minimized, collection instruments are clearly understood, and the impact of collection requirements on respondents can be properly assessed. The purpose of this Notice is to solicit comments concerning the continuance of the Generic Clearance for the Collection of Qualitative Feedback on Agency Service Delivery. A copy of the proposed information collection request can be obtained by contacting the individual listed below in the **ADDRESSES** section of this notice.

DATES: Written comments must be submitted to the office listed in the **ADDRESSES** section below on or before November 12, 2020.

ADDRESSES: Send comments to: Connie Bodner, Ph.D., Director of Grants Policy and Management, Office of Grants Policy and Management, Institute of Museum and Library Services, 955 L'Enfant Plaza North SW, Suite 4000, Washington, DC 20024–2135. Dr. Bodner can be reached by Telephone: 202–653–4636, or by email at *cbodner@imls.gov* or by teletype (TTY/TDD) at 202–653–4614. Office hours are from

8:30 a.m. to 5 p.m., E.T., Monday through Friday, except Federal holidays.

FOR FURTHER INFORMATION CONTACT: Matthew Birnbaum, Ph.D., Supervisory Social Science Researcher, Planning, Research and Evaluation, Institute of Museum and Library Services, 955 L'Enfant Plaza North, SW, Suite 4000, Washington, DC 20024–2135. Dr. Birnbaum can be reached by Telephone: 202–653–4760, Fax: 202– 653–4601, or by email at *mbirnbaum@imls.gov,* or by teletype (TTY/TDD) for persons with hearing difficulty at 202–653–4614.

SUPPLEMENTARY INFORMATION: IMLS is particularly interested in comments that help the agency to:

• 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;

• 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;

• Enhance the quality, utility and clarity of the information to be collected; and

• 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 submissions of responses.

I. Background

The Institute of Museum and Library Services is the primary source of federal support for the nation's libraries and museums. We advance, support, and empower America's museums, libraries, and related organizations through grant making, research, and policy development. Our vision is a nation where museums and libraries work together to transform the lives of individuals and communities. To learn more, visit *www.imls.gov.*

II. Current Actions

This proposed request is to renew IMLS' generic clearance for collection of qualitative feedback on the Agency's service delivery. This data collection activity provides a means to garner qualitative customer and stakeholder feedback in an efficient and timely manner in accordance with the Administration's commitment to improving service delivery. By qualitative feedback, IMLS means information that provides useful insights on perceptions and opinions, but are not statistical surveys that yield quantitative results that can be generalized to the population of study. The Generic Clearance for the Collection of Qualitative Feedback on Agency Service Delivery has been conducted by the Institute of Museum and Library Services under the clearance number 3137–0081, which expires December 31, 2020.

Agency: Institute of Museum and Library Services.

Title: Generic Clearance for the Collection of Qualitative Feedback on Agency Service Delivery.

OMB Number: 3137–0081.

Agency Number: 3137.

Affected Public: State and local governments, State library agencies, and public libraries.

Number of Respondents: 9,854.

Frequency of Response: Once per request.

Average minutes per response: 51 minutes.

Total burden hours: 1,578.

Cost Burden (dollars): $44,095.19.

Public Comments Invited: Comments submitted in response to this notice will be summarized and/or included in the request for OMB's clearance of this information collection.

Dated: September 9, 2020.

Kim Miller,

Senior Grants Management Specialist, Institute of Museum and Library Services.

[FR Doc. 2020–20225 Filed 9–11–20; 8:45 am]

BILLING CODE 7036–01–P

NATIONAL FOUNDATION ON THE ARTS AND THE HUMANITIES

National Endowment for the Humanities

Meeting of Humanities Panel

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

ACTION: Notice of meeting.

SUMMARY: The National Endowment for the Humanities (NEH) will hold fifteen meetings, by videoconference, of the Humanities Panel, a federal advisory committee, during October 2020. The purpose of the meetings is for panel review, discussion, evaluation, and recommendation of applications for financial assistance under the National Foundation on the Arts and the Humanities Act of 1965.

DATES: See **SUPPLEMENTARY INFORMATION** for meeting dates. The meetings will open at 8:30 a.m. and will adjourn by 5:00 p.m. on the dates specified below.

FOR FURTHER INFORMATION CONTACT: Elizabeth Voyatzis, Committee Management Officer, 400 7th Street SW, Room 4060, Washington, DC 20506; (202) 606–8322; *evoyatzis@neh.gov.*

SUPPLEMENTARY INFORMATION: Pursuant to section 10(a)(2) of the Federal Advisory Committee Act (5 U.S.C. App.), notice is hereby given of the following meetings:

1. DATE: October 6, 2020

This video meeting will discuss applications on the topic of Literary Studies, for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

2. DATE: October 8, 2020

This video meeting will discuss applications on the topics of Art and Architectural History, for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

3. DATE: October 14, 2020

This video meeting will discuss applications on the topics of Film and Media Studies, for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

4. DATE: October 15, 2020

This video meeting will discuss applications on the topic of World Studies (Pre-Modern Era), for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

5. DATE: October 19, 2020

This video meeting will discuss applications for the Short Documentaries grant program, submitted to the Division of Public Programs.

6. DATE: October 20, 2020

This video meeting will discuss applications on the topics of World History and Culture, for Media Projects: Production Grants, submitted to the Division of Public Programs.

7. DATE: October 20, 2020

This video meeting will discuss applications on the topic of American Studies, for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

8. DATE: October 22, 2020

This video meeting will discuss applications on the topic of U.S. History (African American Studies), for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

9. DATE: October 22, 2020

This video meeting will discuss applications on the topics of Radio and

Podcasts, for Media Projects: Production Grants, submitted to the Division of Public Programs.

10. DATE: October 23, 2020

This video meeting will discuss applications on the topics of Art History and Culture, for Media Projects: Production Grants, submitted to the Division of Public Programs.

11. DATE: October 26, 2020

This video meeting will discuss applications on the topics of Civics and Society, for Media Projects: Production Grants, submitted to the Division of Public Programs.

12. DATE: October 27, 2020

This video meeting will discuss applications on the topics of U.S. History and Culture, for Media Projects: Production Grants, submitted to the Division of Public Programs.

13. DATE: October 27, 2020

This video meeting will discuss applications on the topic of Art History, for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

14. DATE: October 28, 2020

This video meeting will discuss applications on the topic of U.S. History (West), for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

15. DATE: October 29, 2020

This video meeting will discuss applications on the topics of Music and Performing Arts, for the Humanities Collections and Reference Resources grant program, submitted to the Division of Preservation and Access.

Because these meetings will include review of personal and/or proprietary financial and commercial information given in confidence to the agency by grant applicants, the meetings will be closed to the public pursuant to sections 552b(c)(4) and 552b(c)(6) of Title 5, U.S.C., as amended. I have made this determination pursuant to the authority granted me by the Chairman's Delegation of Authority to Close Advisory Committee Meetings dated April 15, 2016.

Dated: September 8, 2020.

Caitlin Cater,

Attorney-Advisor, National Endowment for the Humanities.

[FR Doc. 2020–20140 Filed 9–11–20; 8:45 am]

BILLING CODE 7536–01–P

NATIONAL SCIENCE FOUNDATION

Agency Information Collection Activities: Comment Request;

Medical Clearance Process for Deployment to the Polar Regions

AGENCY: National Science Foundation.

ACTION: Submission for OMB review; comment request.

SUMMARY: The National Science Foundation (NSF) has submitted the following information collection requirement to OMB for review and clearance under the Paperwork Reduction Act of 1995. This is the *second notice* for public comment; the first was published in the **Federal Register**, and no comments were received. NSF is forwarding the proposed submission to the Office of Management and Budget (OMB) for clearance simultaneously with the publication of this second notice.

DATES: Written comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *www.reginfo.gov/public/do/PRAmain.* Find this particular information collection by selecting ''Currently under 30-day Review—Open for Public Comments'' or by using the search function.

FOR FURTHER INFORMATION CONTACT: Suzanne H. Plimpton, Reports Clearance Officer, National Science Foundation, 2415 Eisenhower Avenue, Alexandria, VA 22314, or send email to *splimpto@nsf.gov.* Individuals who use a telecommunications device for the deaf (TDD) may call the Federal Information Relay Service (FIRS) at 1–800–877–8339, which is accessible 24 hours a day, 7 days a week, 365 days a year (including federal holidays).

Copies of the submission may be obtained by calling 703–292–7556.

SUPPLEMENTARY INFORMATION: NSF 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.

Title of Collection: Medical Clearance Process for Deployment to the Polar Regions.

OMB Number: 3145–0177.

Type of Request: Revision to and extension of approval of an information collection.

Proposed Project: Presidential Memorandum No. 6646 (February 5, 1982) (available from the National Science Foundation, Office of Polar Programs, Suite 755, 4201 Wilson Boulevard, Arlington, VA 22230) sets forth the National Science Foundation's overall management responsibilities for the entire United States national program in Antarctica. Section 107(a) of Public law 98–373 [July 31, 1984; amended as Public Law 101–609–November 16, 1990] [available from the National Science Foundation, Office of Polar Programs, Suite 755, 4201 Wilson Boulevard, Arlington, VA 22230] designates the National Science Foundation as the lead agency responsible for implementing Arctic research policy, and the Director of the National Science Foundation shall ensure that the requirements of section 108 are fulfilled.

NSF Form 1700, Medical Clearance Process for Deployment to the Polar Regions furnishes information to the NSF regarding the physical, dental, and mental health status for all individuals (except DoD-uniformed service personnel) who anticipate deploying to Antarctica under the auspices of the United States Antarctic Program or to certain regions of the Arctic sponsored by the NSF/GEO/Office of Polar Programs. The information is used to determine whether an individual is physically and mentally suited to endure the extreme hardships imposed by the Arctic and Antarctic continents, while also performing specific duties as specified by their employers.

Respondents: All non-DoD uniformed personnel planning to deploy to U.S. stations in the Antarctic or to specified regions of the Arctic that are sponsored by the National Science Foundation's Office of Polar Programs.

The number of Annual Respondents: 3,500 to the Antarctic and 150 to the Arctic.

Estimated Total Annual Burden on Respondents: 36,500 hours.

Frequency of Responses: This form is submitted upon an individual's first deployment to Antarctica (below 60° South) or to specified regions of the Arctic and annually thereafter for the duration of the individual's deployments.

Comments: Comments are invited on (a) whether the proposed collection of information is necessary for the proper performance of the functions of the Agency, including whether the information shall have practical utility; (b) the accuracy of the Agency's estimate of the burden of the proposed collection of information; (c) ways to enhance the quality, utility, and clarity of the information on respondents, including through the use of automated collection techniques or other forms of information technology; and (d) 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.

Dated: September 9, 2020.

Suzanne H. Plimpton,

Reports Clearance Officer, National Science Foundation.

[FR Doc. 2020–20227 Filed 9–11–20; 8:45 am]

BILLING CODE 7555–01–P

NUCLEAR REGULATORY COMMISSION

[NRC–2020–0040]

Information Collection: DOE/NRC Form 740M, Concise Note; DOE/NRC Form 741, Nuclear Material Transaction Report; DOE/NRC Form 742, Material Balance Report; and DOE/NRC Form 742C, Physical Inventory Listing

AGENCY: Nuclear Regulatory Commission.

ACTION: Notice of submission to the Office of Management and Budget; request for comment.

SUMMARY: The U.S. Nuclear Regulatory Commission (NRC) has recently submitted a request for renewal of an existing collection of information to the Office of Management and Budget (OMB) for review. The information collections are entitled, ''DOE/NRC Form 740M, Concise Note; DOE/NRC Form 741, Nuclear Material Transaction Report; DOE/NRC Form 742, Material Balance Report; and DOE/NRC Form 742C, Physical Inventory Listing.''

DATES: Submit comments by October 14, 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: Written comments and recommendations for the proposed information collection should be sent within 30 days of publication of this notice to *https://www.reginfo.gov/public/do/PRAMain.* Find this particular information collection by selecting ''Currently under Review—Open for Public Comments'' or by using the search function.

FOR FURTHER INFORMATION CONTACT: David Cullison, NRC Clearance 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–2020–0040 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–2020–0040. A copy of the collection of information and related instructions may be obtained without charge by accessing Docket ID NRC–2020–0040 on this website.
- *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 select ''*Begin Web-based ADAMS Search.*'' For problems with ADAMS, please contact the NRC's Public Document Room reference staff at 1–800–397–4209, 301–415–4737, or by email to *pdr.resource@nrc.gov.* For the convenience of the reader, instructions about obtaining materials referenced in this document are provided in the ''Availability of Documents'' section.
- *NRC's Clearance Officer:* A copy of the collection of information and related instructions may be obtained without charge by contacting the 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

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. All comment submissions are posted at *https://www.regulations.gov* and entered into ADAMS. Comment submissions are not routinely edited to remove identifying or contact information.

If you are requesting or aggregating comments from other persons for submission to the OMB, 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 comment submissions are not routinely edited to remove such information before making the comment submissions available to the public or entering the comment into ADAMS.

II. Background

Under the provisions of the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35), the NRC recently submitted a request for renewal of an existing collection of information to OMB for review entitled, ''DOE/NRC Form 740M, Concise Note; DOE/NRC Form 741, Nuclear Material Transaction Report; DOE/NRC Form 742, Material Balance Report; and DOE/NRC Form 742C, Physical Inventory Listing.'' The NRC hereby informs potential respondents that an agency may not conduct or sponsor, and that a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

The NRC published a **Federal Register** notice with a 60-day comment period on this information collection on April 29, 2020, (85 FR 23870).

1. *The title of the information collection:* DOE/NRC Form 740M, Concise Note; DOE/NRC Form 741, Nuclear Material Transaction Report; DOE/NRC Form 742, Material Balance Report; and DOE/NRC Form 742C, Physical Inventory Listing.
2. *OMB approval number:* DOE/NRC Form 740M: 3150–0057. DOE/NRC Form 741: 3150–0003. DOE/NRC Form 742: 3150–0004. DOE/NRC Form 742C: 3150–0058.
3. *Type of submission:* Extension.
4. *The form number if applicable:* DOE/NRC Forms 740M, 741, 742, and 742C.
5. *How often the collection is required or requested:* DOE/NRC Form 741, Nuclear Material Transaction Reports will be collected whenever nuclear material is shipped or received into the Material Balance Area; DOE/NRC Form 742, Material Balance Report will be collected on an annual basis; DOE/NRC Form 742C, Physical Inventory Listing will be collected on an annual basis; DOE/NRC Form 740M, Concise Note Forms are used when needed.
6. *Who will be required or asked to respond:* Persons licensed to possess specified quantities of nuclear material and entities subject to the U.S.-IAEA Caribbean Territories Safeguards Agreement (INFCIRC/366) are required to respond as follows:

Any licensee who ships, receives, or otherwise undergoes an inventory change of nuclear material is required to submit a DOE/NRC Form 741 to document the change. Additional information regarding these transactions shall be submitted through Form 740M, with Safeguards Information identified and handled in accordance with section 73.21 of title 10 of the *Code of Federal Regulations,* ''Requirements for the Protection of Safeguards Information.''

Any licensee who had possessed in the previous reporting period, at any one time and location, nuclear material in a quantity totaling one gram or more shall complete DOE/NRC Form 742. In addition, each licensee, Federal or State, who is authorized to possess, at any one time or location, one kilogram of foreign obligated source material, is required to file with the NRC an annual statement of source material inventory which is foreign obligated.

Any licensee, who had possessed in the previous reporting period, at any one time and location, special nuclear material in a quantity totaling one gram or more shall complete DOE/NRC Form 742C.

7. *The estimated number of annual responses:*

DOE/NRC Form 740M: 175.
DOE/NRC Form 741: 11,143.
DOE/NRC Form 742: 344.
DOE/NRC Form 742C: 385.

8. *The estimated number of annual respondents:*

DOE/NRC Form 740M: 40.
DOE/NRC Form 741: 344.
DOE/NRC Form 742: 344.
DOE/NRC Form 742C: 385.

9. *The estimated number of hours needed annually to comply with the information collection requirement or request:*

DOE/NRC Form 740M: 131.
DOE/NRC Form 741: 13,928.
DOE/NRC Form 742: 1,204.
DOE/NRC Form 742C: 1,490.

10. *Abstract:* Persons licensed to possess specified quantities of nuclear material currently report inventory and transaction of material to the Nuclear Materials Management and Safeguards System via the DOE/NRC Forms: DOE/NRC Form 740M, Concise Note; DOE/NRC Form 741, Nuclear Material Transaction Report; DOE/NRC Form 742, Material Balance Report; and DOE/NRC Form 742C, Physical Inventory Listing. This collection is being revised to include approximately 25 entities subject to the U.S.-IAEA Caribbean Territories Safeguards Agreement (INFCIRC/366). Part 75 requires licensees to provide reports of nuclear material inventory and flow for entities under the U.S.-IAEA Caribbean Territories Safeguards Agreement (INFCIRC/366), permit inspections by Agreement (INFCIRC/366). The IAEA inspectors, give immediate notice to the NRC in specified situations involving the possibility of loss of nuclear material, and give notice for imports and exports of specified amounts of nuclear material. These licensees will also follow written material accounting and control procedures. Reporting of transfer and material balance records to the IAEA will be done through the U.S. State system (Nuclear Materials Management and Safeguards System, collected under OMB clearance numbers 3150–0003, 3150–0004, 3150–0057, and 3150–0058.) The NRC needs this information to implement its international obligations under the U.S.-IAEA Caribbean Territories Safeguards.

III. Availability of Documents

The supplemental documents related to each information collections are identified in the following table and are available to interested persons in ADAMS.

DOCUMENTS	ADAMS Accession No.
Supporting statement and DOE/NRC Form 740M, ''Concise Note'' (3150–0057).	ML20183A141 and ML20021A120.
Supporting statement and DOE/NRC Form 741, ''Nuclear Material Transaction Report'' (3150–0003).	ML20183A140 and ML20021A121.
Supporting statement and DOE/NRC Form 742, ''Material Balance Report'' (3150–0004).	ML20183A186 and ML20024D128.
Supporting statement and DOE/NRC Form 742C, ''Physical Inventory Listing''.	ML20183A187 and ML20024D129.
(3150–0058)	
NUREG/BR–0006, Revision 9 (3150–0003; 3150–0057)	ML20240A155.
NUREG/BR–0007, Revision 7 (3150–0004; 3150–0058)	ML18123A462.
D–24 Personal Computer Data Input for Nuclear Regulatory Commission Licensees.	ML20092K107.

Dated: September 8, 2020.

For the Nuclear Regulatory Commission.

David C. Cullison,

NRC Clearance Officer, Office of the Chief Information Officer.

[FR Doc. 2020–20138 Filed 9–11–20; 8:45 am]

BILLING CODE 7590–01–P

PUBLIC BUILDINGS REFORM BOARD

Notice of Public Meeting: Progress on Selling the High Value Assets and Preparations for the Upcoming First Round of Recommendations, etc.

AGENCY: Public Buildings Reform Board.

ACTION: Notice of public meeting.

SUMMARY: As provided by the Federal Assets Sale and Transfer Act of 2016 (FASTA), the Public Buildings Reform Board (PBRB) is holding a meeting to discuss its progress on the High Value Asset Round and preparations for the upcoming First Round of sales, consolidations, property disposals, and redevelopment recommendations.

DATES: The meeting is scheduled for Thursday, October 1st, 2020, from 2:00 p.m. to 4:00 p.m. (Eastern Daylight Time).

ADDRESSES: Due to public health concerns driven by the COVID–19 pandemic, this meeting will be open to the public virtually via WebEx video conferencing. Interested participants must register to attend for the public meeting via this link: *https://jllmeet.webex.com/jllmeet/onstage/g.php?MTID=e56b82ebae21118cbb2919c9853546c19*.

Those who require special assistance or accommodations in order to attend must contact the PBRB Team at *fastainfo@pbrb.gov* at least 12 days prior to the event.

FOR FURTHER INFORMATION CONTACT: Questions and comments can be forwarded to the PBRB Team by email at *fastainfo@pbrb.gov*. Or you may contact Courtney Johnson at (301) 357–3981 or *courtney.d.johnson@pbrb.gov*.

SUPPLEMENTARY INFORMATION:

Background

FASTA created the PBRB as an independent Board to identify opportunities for the Federal government to significantly reduce its inventory of civilian real property and thereby reduce costs. The Board is directed, within 6 months of its formation, to recommend to the Office of Management and Budget (OMB) the sale of not fewer than five properties not on the list of surplus or excess with a fair market value of not less than $500 million and not more than $750 million. In two subsequent rounds over a five-year period, the Board is responsible for making recommendations for other sales, consolidations, property disposals or redevelopment of up to $7.25 billion in value.

Format and Registration

The format for the meeting will be panel discussions with appropriate time allowed for a Q&A segment. Interested participants must register to attend for the public meeting via this link: *https://jllmeet.webex.com/jllmeet/onstage/g.php?MTID=e56b82ebae21118cbb2919c9853546c19.*

Those who require special assistance or accommodations in order to attend must contact the PBRB Team at *fastainfo@pbrb.gov* at least 12 days prior to the event.

Portions of the meeting may be held in executive session if the Board is considering issues involving classified or proprietary information.

A transcript of the public meeting will be available at pbrb.gov following the session.

If you have any additional questions please email *fastainfo@pbrb.gov.*

Authority: Pub. L. 114–287, 130 Stat 1463.

Courtney Johnson,

Federal Register Liaison, Public Buildings Reform Board.

[FR Doc. 2020–20175 Filed 9–11–20; 8:45 am]

BILLING CODE P

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89778; File No. SR–CboeBYX–2020–025

Self-Regulatory Organizations; Cboe BYX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Rule 11.26(a), Stating It Will Utilize MIAX PEARL Market Data From the CQSUQDF for Purposes of Order Handling, Routing, Execution, and Related Compliance Processes

September 8, 2020.

Pursuant to Section 19(b)(1) [1] of the Securities Exchange Act of 1934 (the ''Act'') [2] and Rule 19b–4 thereunder,[3] notice is hereby given that on August 25, 2020, Cboe BYX Exchange, Inc. (the ''Exchange'' or ''BYX'') filed with the Securities and Exchange Commission (the ''Commission'') the proposed rule change as described in Items I and II 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

Cboe BYX Exchange, Inc. (''BYX'' or the ''Exchange'') proposes to update Rule 11.26(a), stating it will utilize MIAX PEARL market data from the CQSUQDF for purposes of order handling, routing, execution, and related compliance processes. The text of the proposed rule change is provided in Exhibit 5.

The text of the proposed rule change is also available on the Exchange's website (*http://markets.cboe.com/us/equities/regulation/rule_filings/byx/*), at the Exchange's Office of the Secretary, 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to update Rule 11.26(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of the MIAX PEARL as an equities exchange.

On August 14, 2020, the Commission approved MIAX PEARL's proposed rule change to establish rules governing the trading of equities securities.[4] MIAX PEARL announced that it plans to launch equities trading on September 25, 2020.[5] The Exchange, therefore, proposes to update Rule 11.26(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of MIAX PEARL as an equities exchange beginning on September 25, 2020. Specifically, the Exchange proposes to amend Rule 11.26(a) to include MIAX PEARL by stating it will utilize MIAX PEARL market data from the Consolidated Quotation System (''CQS'')/UTP Quotation Data Feed (''UQDF'') for purposes of order handling, routing, execution, and related compliance processes. At this stage, no secondary source for MIAX PEARL market data will be used.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[6] in general, and furthers the objectives of Section 6(b)(5) of the Act,[7] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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.

The Exchange believes that its proposal to update Exchange Rule 11.26(a) to include MIAX PEARL will ensure that the Rule correctly identifies and publicly states on a market-by-market basis all of the specific network processor and proprietary data feeds that the Exchange utilizes for the handling, routing, and execution of orders, and for performing the regulatory compliance checks related to each of those functions. The proposed rule changes also remove impediments to and perfects the mechanism of a free and open market and protects investors and the public interest because it provides additional specificity, clarity and transparency.

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

[4] *See* Securities Exchange Act No. 89562 (August 14, 2020).

[5] *See supra* note 3 [sic].

[6] 15 U.S.C. 78f.

[7] 15 U.S.C. 78f(b)(5).

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange believes its proposed rule change would not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. To the contrary, the Exchange believes the proposal would enhance competition because including all of the exchanges enhances transparency and enables investors to better assess the quality of the Exchange's execution and routing services.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from Members or other interested parties.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

(i) Significantly affect the protection of investors or the public interest;

(ii) impose any significant burden on competition; and

(iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act [8] and Rule 19b–4(f)(6) thereunder.[9]

At any time within 60 days of the filing of the 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.

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–CboeBYX–2020–025 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–CboeBYX–2020–025. 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–CboeBYX–2020–025 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[10]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20124 Filed 9–11–20; 8:45 am]

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[8] 15 U.S.C. 78s(b)(3)(A).

[9] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has fulfilled this requirement.

[10] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89788; File No. 4–678]

Program for Allocation of Regulatory Responsibilities Pursuant to Rule 17d–2; Notice of Filing and Order Approving and Declaring Effective an Amended Proposed Plan for the Allocation of Regulatory Responsibilities Among the Financial Industry Regulatory Authority, Inc., Miami International Securities Exchange, LLC, MIAX PEARL, LLC, and MIAX Emerald, LLC

September 8, 2020.

Notice is hereby given that the Securities and Exchange Commission (''Commission'') has issued an Order, pursuant to Section 17(d) of the Securities Exchange Act of 1934 (''Act''),[1] approving and declaring effective an amendment to the plan for allocating regulatory responsibility (''Plan'') filed on September 2, 2020, pursuant to Rule 17d–2 of the Act,[2] by the Miami International Securities Exchange, LLC (''MIAX''), MIAX PEARL, LLC (''MIAX PEARL''), MIAX Emerald, LLC (''MIAX Emerald'') and the Financial Industry Regulatory Authority, Inc. (''FINRA'') (together, the ''Parties''). The Plan replaces and supersedes the agreement entered into between FINRA, MIAX and MIAX PEARL on December 19, 2018, entitled ''Agreement between Financial Industry Regulatory Authority, Inc., Miami International Securities Exchange, LLC and MIAX PEARL, LLC Pursuant to Rule 17d–2 under the Securities Exchange Act of 1934.'' [3]

I. Introduction

Section 19(g)(1) of the Securities Exchange Act of 1934 (''Act''),[4] among other things, requires every self-regulatory organization (''SRO'') registered as either a national securities exchange or national securities association to examine for, and enforce compliance by, its members and persons associated with its members with the Act, the rules and regulations thereunder, and the SRO's own rules, unless the SRO is relieved of this responsibility pursuant to Section 17(d) or Section 19(g)(2) of the Act.[5] Without this relief, the statutory obligation of each individual SRO could result in a

[1] 15 U.S.C. 78q(d).

[2] 17 CFR 240.17d–2.

[3] *See* Securities Exchange Act Release No. 85189 (February 25, 2019), 84 FR 7153 (March 1, 2019).

[4] 15 U.S.C. 78s(g)(1).

[5] 15 U.S.C. 78q(d) and 15 U.S.C. 78s(g)(2), respectively.

pattern of multiple examinations of broker-dealers that maintain memberships in more than one SRO (''common members''). Such regulatory duplication would add unnecessary expenses for common members and their SROs.

Section 17(d)(1) of the Act [6] was intended, in part, to eliminate unnecessary multiple examinations and regulatory duplication.[7] With respect to a common member, Section 17(d)(1) authorizes the Commission, by rule or order, to relieve an SRO of the responsibility to receive regulatory reports, to examine for and enforce compliance with applicable statutes, rules, and regulations, or to perform other specified regulatory functions.

To implement Section 17(d)(1), the Commission adopted two rules: Rule 17d–1 and Rule 17d–2 under the Act.[8] Rule 17d–1 authorizes the Commission to name a single SRO as the designated examining authority (''DEA'') to examine common members for compliance with the financial responsibility requirements imposed by the Act, or by Commission or SRO rules.[9] When an SRO has been named as a common member's DEA, all other SROs to which the common member belongs are relieved of the responsibility to examine the firm for compliance with the applicable financial responsibility rules. On its face, Rule 17d–1 deals only with an SRO's obligations to enforce member compliance with financial responsibility requirements. Rule 17d–1 does not relieve an SRO from its obligation to examine a common member for compliance with its own rules and provisions of the federal securities laws governing matters other than financial responsibility, including sales practices and trading activities and practices.

To address regulatory duplication in these and other areas, the Commission adopted Rule 17d–2 under the Act.[10] Rule 17d–2 permits SROs to propose joint plans for the allocation of regulatory responsibilities with respect to their common members. Under paragraph (c) of Rule 17d–2, the Commission may declare such a plan effective if, after providing for appropriate notice and comment, it determines that the plan is necessary or appropriate in the public interest and for the protection of investors; to foster cooperation and coordination among the SROs; to remove impediments to, and foster the development of, a national market system and a national clearance and settlement system; and is in conformity with the factors set forth in Section 17(d) of the Act. Commission approval of a plan filed pursuant to Rule 17d–2 relieves an SRO of those regulatory responsibilities allocated by the plan to another SRO.

II. The Plan

On November 19, 2014, the Commission declared effective the Plan entered into between FINRA and MIAX for allocating regulatory responsibility pursuant to Rule 17d–2.[11] The Plan is intended to reduce regulatory duplication for firms that are common members of both MIAX and FINRA. The plan reduces regulatory duplication for firms that are members of MIAX and FINRA by allocating regulatory responsibility with respect to certain applicable laws, rules, and regulations. Included in the Plan is an exhibit that lists every MIAX rule for which FINRA bears responsibility under the Plan for overseeing and enforcing with respect to MIAX members that are also members of FINRA and the associated persons therewith. On January 12, 2017, the parties submitted a proposed amendment to the Plan to add MIAX PEARL as a Participant to the Plan.[12] On June 28, 2018, the parties submitted a proposed amendment to the Plan to allocate surveillance, investigation, and enforcement responsibilities for Rule 14e–4 under the Act, as well as certain provisions of Regulation SHO.[13] On December 20, 2018, the parties submitted a proposed amendment to the Plan to add MIAX EMERALD as a Participant to the Plan.[14]

III. Proposed Amendment to the Plan

On September 2, 2020, the parties submitted a proposed amendment to the Plan (''Amended Plan''). The primary purpose of the Amended Plan is to add MIAX PEARL equities rules and certain federal securities laws to the Certification. The text of the proposed Amended Plan is as follows (additions are *italicized;* deletions are [bracketed]):

Agreement Among Financial Industry Regulatory Authority, Inc., Miami International Securities Exchange, LLC, MIAX Pearl, LLC and MIAX Emerald, LLC Pursuant to Rule 17d–2 Under the Securities Exchange Act of 1934

This Agreement, by and among the Financial Industry Regulatory Authority, Inc. (''FINRA''), Miami International Securities Exchange, LLC (''MIAX''), MIAX PEARL, LLC (''MIAX PEARL''), and MIAX Emerald, LLC (''MIAX Emerald'') is made this 2nd day of September, 2020 (the ''Agreement''), pursuant to Section 17(d) of the Securities Exchange Act of 1934 (the ''Exchange Act'') and Rule 17d–2 thereunder, which permits agreements between self-regulatory organizations to allocate regulatory responsibility to eliminate regulatory duplication. FINRA, MIAX, MIAX PEARL and MIAX Emerald may be referred to individually as a ''party'' and together as the ''parties.''

This Agreement amends and restates the agreement entered into between FINRA, MIAX and MIAX PEARL on December 19, 2018, entitled ''Agreement between Financial Industry Regulatory Authority, Inc., Miami International Securities Exchange, LLC and MIAX PEARL, LLC Pursuant to Rule 17d–2 under the Securities Exchange Act of 1934,'' and any subsequent amendments thereafter.

Whereas, the parties desire to reduce duplication in the examination and surveillance of their Common Members (as defined herein) and in the filing and processing of certain registration and membership records; and

Whereas, the parties desire to execute an agreement covering such subjects pursuant to the provisions of Rule 17d–2 under the Exchange Act and to file such agreement with the Securities and Exchange Commission (the ''SEC'' or ''Commission'') for its approval.

Now, therefore, in consideration of the mutual covenants contained hereinafter, the parties hereby agree as follows:

1. *Definitions.* Unless otherwise defined in this Agreement or the context otherwise requires, the terms used in this Agreement shall have the same meaning as they have under the Exchange Act and the rules and regulations thereunder. As used in this Agreement, the following terms shall have the following meanings:

(a) ''*MIAX Rules,*'' ''*MIAX PEARL Rules*'', ''*MIAX Emerald Rules*'' or ''*FINRA Rules*'' shall mean: (i) The rules of MIAX, MIAX PEARL or MIAX

[6] 15 U.S.C. 78q(d)(1).

[7] *See* Securities Act Amendments of 1975, Report of the Senate Committee on Banking, Housing, and Urban Affairs to Accompany S. 249, S. Rep. No. 94–75, 94th Cong., 1st Session 32 (1975).

[8] 17 CFR 240.17d–1 and 17 CFR 240.17d–2, respectively.

[9] *See* Securities Exchange Act Release No. 12352 (April 20, 1976), 41 FR 18808 (May 7, 1976).

[10] *See* Securities Exchange Act Release No. 12935 (October 28, 1976), 41 FR 49091 (November 8, 1976).

[11] *See* Securities Exchange Act Release No. 73641 (November 19, 2014), 79 FR 70230 (November 25, 2014).

[12] *See* Securities Exchange Act Release Nos. 79779 (January 12, 2017), 82 FR 6674 (January 19, 2017) (notice) and 79974 (February 6, 2017), 82 FR 10417 (February 10, 2017) (order).

[13] *See* Securities Exchange Act Release No. 83696 (July 24, 2018), 83 FR 35682 (July 27, 2018).

[14] *See* Securities Exchange Act Release No. 85189 (February 25, 2019), 84 FR 7153 (March 1, 2019).

Emerald, respectively, or (ii) the rules of FINRA, respectively, as the rules of an exchange or association are defined in Exchange Act Section 3(a)(27).

(b) ''*Common Rules*'' shall mean MIAX Rules, MIAX PEARL Rules and MIAX Emerald Rules that are substantially similar to the applicable FINRA Rules and certain provisions of the Exchange Act and SEC rules set forth on Exhibit 1 in that examination or surveillance for compliance with such provisions and rules would not require FINRA to develop one or more new examination or surveillance standards, modules, procedures, or criteria in order to analyze the application of the provision or rule, or a Common Member's activity, conduct, or output in relation to such provision or rule; provided, however, Common Rules shall not include the application of the SEC, MIAX PEARL or FINRA rules as they pertain to violations of insider trading activities, which is covered by a separate 17d–2 Agreement by and among Cboe BZX Exchange, Inc., Cboe BYX Exchange, Inc., Chicago Stock Exchange, Inc., Cboe EDGA Exchange, Inc., Cboe EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., MEMX, LLC, Nasdaq BX, Inc., Nasdaq PHLX LLC, The Nasdaq Stock Market LLC, NYSE National, Inc., New York Stock Exchange LLC, NYSE American LLC, NYSE Arca Inc., Investors' Exchange LLC and Long-Term Stock Exchange, Inc. effective May 26, 2020, as may be amended from time to time. Common Rules shall not include any provisions regarding (i) notice, reporting or any other filings made directly to or from MIAX, MIAX PEARL or MIAX Emerald, (ii) incorporation by reference of other MIAX, MIAX PEARL Rules or MIAX Emerald Rules that are not Common Rules, (iii) exercise of discretion in a manner that differs from FINRA's exercise of discretion including, but not limited to exercise of exemptive authority, by MIAX, MIAX PEARL or MIAX Emerald, (iv) prior written approval of MIAX, MIAX PEARL or MIAX Emerald and (v) payment of fees or fines to MIAX, MIAX PEARL or MIAX Emerald.

(c) ''*Common Members*'' shall mean members of FINRA and at least one of MIAX, MIAX PEARL or MIAX Emerald.

(d) ''*Effective Date*'' shall be the date this Agreement is approved by the Commission.

(e) ''*Enforcement Responsibilities*'' shall mean the conduct of appropriate proceedings, in accordance with FINRA's Code of Procedure (the Rule 9000 Series) and other applicable FINRA procedural rules, to determine whether violations of Common Rules have occurred, and if such violations are deemed to have occurred, the imposition of appropriate sanctions as specified under FINRA's Code of Procedure and sanctions guidelines.

(f) ''*Regulatory Responsibilities*'' shall mean the examination responsibilities, surveillance responsibilities and Enforcement Responsibilities relating to compliance by the Common Members with the Common Rules and the provisions of the Exchange Act and the rules and regulations thereunder, and other applicable laws, rules and regulations, each as set forth on *Exhibit 1* attached hereto.

2. *Regulatory and Enforcement Responsibilities.* FINRA shall assume Regulatory Responsibilities and Enforcement Responsibilities for Common Members. Attached as *Exhibit 1* to this Agreement and made part hereof, MIAX, MIAX PEARL and MIAX Emerald furnished FINRA with a current list of Common Rules and certified to FINRA that such rules that are MIAX Rules, MIAX PEARL Rules and MIAX Emerald Rules are substantially similar to the corresponding FINRA Rules (the ''Certification''). FINRA hereby agrees that the rules listed in the Certification are Common Rules as defined in this Agreement. Each year following the Effective Date of this Agreement, or more frequently if required by changes in the rules of the parties, MIAX, MIAX PEARL and MIAX Emerald shall submit an updated list of Common Rules to FINRA for review which shall add MIAX Rules, MIAX PEARL Rules or MIAX Emerald Rules not included in the current list of Common Rules that qualify as Common Rules as defined in this Agreement; delete MIAX Rules, MIAX PEARL Rules or MIAX Emerald Rules included in the current list of Common Rules that no longer qualify as Common Rules as defined in this Agreement; and confirm that the remaining rules on the current list of Common Rules continue to be MIAX Rules, MIAX PEARL Rules or MIAX Emerald Rules that qualify as Common Rules as defined in this Agreement. Within 30 days of receipt of such updated list, FINRA shall confirm in writing whether the rules listed in any updated list are Common Rules as defined in this Agreement. Notwithstanding anything herein to the contrary, it is explicitly understood that the term ''Regulatory Responsibilities'' does not include, and MIAX, MIAX PEARL and MIAX Emerald shall retain full responsibility for (unless otherwise addressed by separate agreement or rule) (collectively, the ''Retained Responsibilities'') the following:

(a) Surveillance, examination, investigation and enforcement with respect to trading activities or practices involving MIAX's, MIAX PEARL's and MIAX Emerald's own marketplace;

(b) registration pursuant to their applicable rules of associated persons (*i.e.,* registration rules that are not Common Rules);

(c) discharge of their duties and obligations as a Designated Examining Authority pursuant to Rule 17d–1 under the Exchange Act; and

(d) any MIAX Rules, MIAX PEARL Rules or MIAX Emerald Rules that are not Common Rules as provided in paragraph 6.

3. *Common Members.* Prior to the Effective Date, MIAX, MIAX PEARL and MIAX Emerald shall furnish FINRA with a current list of Common Members, which shall be updated no less frequently than once each quarter.

4. *No Charge.* There shall be no charge to MIAX, MIAX PEARL and MIAX Emerald by FINRA for performing the Regulatory Responsibilities and Enforcement Responsibilities under this Agreement except as hereinafter provided. FINRA shall provide MIAX, MIAX PEARL and MIAX Emerald with ninety (90) days advance written notice in the event FINRA decides to impose any charges to MIAX, MIAX PEARL and MIAX Emerald for performing the Regulatory Responsibilities under this Agreement. If FINRA determines to impose a charge, MIAX, MIAX PEARL and MIAX Emerald shall have the right at the time of the imposition of such charge to terminate this Agreement; provided, however, that FINRA's Regulatory Responsibilities under this Agreement shall continue until the Commission approves the termination of this Agreement.

5. *Applicability of Certain Laws, Rules, Regulations or Orders.* Notwithstanding any provision hereof, this Agreement shall be subject to any statute, or any rule or order of the SEC. To the extent such statute, rule or order is inconsistent with one or more provisions of this Agreement, the statute, rule or order shall supersede the provision(s) hereof to the extent necessary to be properly effectuated and the provision(s) hereof in that respect shall be null and void.

6. *Notification of Violations.* In the event that FINRA becomes aware of apparent violations of any MIAX Rules, MIAX PEARL Rules or MIAX Emerald Rules, which are not listed as Common Rules, discovered pursuant to the performance of the Regulatory Responsibilities assumed hereunder,

FINRA shall notify MIAX, MIAX PEARL and MIAX Emerald of those apparent violations for such response as MIAX, MIAX PEARL and MIAX Emerald deem appropriate. In the event that MIAX, MIAX PEARL or MIAX Emerald becomes aware of apparent violations of any Common Rules, discovered pursuant to the performance of the Retained Responsibilities, MIAX, MIAX PEARL and MIAX Emerald shall notify FINRA of those apparent violations and such matters shall be handled by FINRA as provided in this Agreement. Apparent violations of Common Rules shall be processed by, and enforcement proceedings in respect thereto shall be conducted by FINRA as provided hereinbefore; provided, however, that in the event a Common Member is the subject of an investigation relating to a transaction on MIAX, MIAX PEARL or MIAX Emerald, MIAX, MIAX PEARL and MIAX Emerald may in their discretion assume concurrent jurisdiction and responsibility. Each party agrees to make available promptly all files, records and witnesses necessary to assist the other in its investigation or proceedings.

7. *Continued Assistance.*

(a) FINRA shall make available to MIAX, MIAX PEARL and MIAX Emerald all information obtained by FINRA in the performance by it of the Regulatory Responsibilities hereunder with respect to the Common Members subject to this Agreement. In particular, and not in limitation of the foregoing, FINRA shall furnish MIAX, MIAX PEARL and MIAX Emerald any information it obtains about Common Members which reflects adversely on their financial condition. MIAX, MIAX PEARL and MIAX Emerald shall make available to FINRA any information coming to its attention that reflects adversely on the financial condition of Common Members or indicates possible violations of applicable laws, rules or regulations by such firms.

(b) The parties agree that documents or information shared shall be held in confidence, and used only for the purposes of carrying out their respective regulatory obligations. No party shall assert regulatory or other privileges as against any other with respect to documents or information that is required to be shared pursuant to this Agreement.

(c) The sharing of documents or information among the parties pursuant to this Agreement shall not be deemed a waiver as against third parties of regulatory or other privileges relating to the discovery of documents or information.

8. *Statutory Disqualifications.* When FINRA becomes aware of a statutory disqualification as defined in the Exchange Act with respect to a Common Member, FINRA shall determine pursuant to Sections 15A(g) and/or Section 6(c) of the Exchange Act the acceptability or continued applicability of the person to whom such disqualification applies and keep MIAX, MIAX PEARL and MIAX Emerald advised of its actions in this regard for such subsequent proceedings as MIAX, MIAX PEARL and MIAX Emerald may initiate.

9. *Customer Complaints.* MIAX, MIAX PEARL and MIAX Emerald shall forward to FINRA copies of all customer complaints involving Common Members received by MIAX, MIAX PEARL and MIAX Emerald relating to FINRA's Regulatory Responsibilities under this Agreement. It shall be FINRA's responsibility to review and take appropriate action in respect to such complaints.

10. *Advertising.* FINRA shall assume responsibility to review the advertising of Common Members subject to the Agreement, provided that such material is filed with FINRA in accordance with FINRA's filing procedures and is accompanied with any applicable filing fees set forth in FINRA Rules.

11. *No Restrictions on Regulatory Action.* Nothing contained in this Agreement shall restrict or in any way encumber the right of any party to conduct its own independent or concurrent investigation, examination or enforcement proceeding of or against Common Members, as any party, in its sole discretion, shall deem appropriate or necessary.

12. *Termination.* This Agreement may be terminated by any party at any time upon the approval of the Commission after one (1) year's written notice to the other parties (or such shorter time as agreed by the parties), except as provided in paragraph 4.

13. *Arbitration.* In the event of a dispute among the parties as to the operation of this Agreement, the parties hereby agree that any such dispute shall be settled by arbitration in Washington, DC in accordance with the rules of the American Arbitration Association then in effect, or such other procedures as the parties may mutually agree upon. Judgment on the award rendered by the arbitrator(s) may be entered in any court having jurisdiction. Each party acknowledges that the timely and complete performance of its obligations pursuant to this Agreement is critical to the business and operations of the other parties. In the event of a dispute among the parties, the parties shall continue to perform their respective obligations under this Agreement in good faith during the resolution of such dispute unless and until this Agreement is terminated in accordance with its provisions. Nothing in this Section 13 shall interfere with a party's right to terminate this Agreement as set forth herein.

14. *Separate Agreement.* This Agreement is wholly separate from the following agreement: (1) The multiparty Agreement made pursuant to Rule 17d–2 of the Exchange Act among Cboe BZX Exchange, Inc., BOX Options Exchange, LLC, Cboe Exchange, Inc., Cboe C2 Exchange, Inc., Nasdaq ISE, LLC, FINRA, MIAX, NYSE American LLC, NYSE Arca, Inc., The Nasdaq Stock Market LLC, Nasdaq BX, Inc., the Nasdaq PHLX LLC, Nasdaq GEMX, LLC, Cboe EDGX Exchange, Inc., Nasdaq MRX, LLC, MIAX PEARL, LLC and MIAX Emerald, LLC involving the allocation of regulatory responsibilities with respect to common members for compliance with common rules relating to the conduct by broker-dealers of accounts for listed options or index warrants entered as approved by the SEC on February 12, 2019, and as may be amended from time to time; and (2) the multiparty Agreement made pursuant to Rule 17d–2 of the Exchange Act among Cboe BZX Exchange, Inc., BOX Options Exchange, LLC, Cboe Exchange, Inc., Cboe C2 Exchange, Inc., Nasdaq ISE, LLC, FINRA, MIAX, NYSE American LLC, NYSE Arca, Inc., The Nasdaq Stock Market LLC, Nasdaq BX, Inc., the Nasdaq PHLX LLC, Nasdaq GEMX, LLC, Cboe EDGX Exchange, Inc., Nasdaq MRX, LLC, MIAX PEARL, LLC and MIAX Emerald, LLC involving the allocation of regulatory responsibilities with respect to SRO market surveillance of common members activities with regard to certain common rules relating to listed options approved by the SEC on February 11, 2019, and as may be amended from time to time.

15. *Notification of Members.* The parties shall notify Common Members of this Agreement after the Effective Date by means of a uniform joint notice.

16. *Amendment.* This Agreement may be amended in writing provided that the changes are approved by each party. All such amendments must be filed with and approved by the Commission before they become effective.

17. *Limitation of Liability.* None of the parties nor any of their respective directors, governors, officers or employees shall be liable to any other party to this Agreement for any liability, loss or damage resulting from or claimed to have resulted from any delays, inaccuracies, errors or omissions

with respect to the provision of Regulatory Responsibilities as provided hereby or for the failure to provide any such responsibility, except with respect to such liability, loss or damages as shall have been suffered by any party and caused by the willful misconduct of another party or their respective directors, governors, officers or employees. No warranties, express or implied, are made by any party hereto with respect to any of the responsibilities to be performed by them hereunder.

18. *Relief from Responsibility.* Pursuant to Sections 17(d)(1)(A) and 19(g) of the Exchange Act and Rule 17d–2 thereunder, FINRA, MIAX, MIAX PEARL and MIAX Emerald join in requesting the Commission, upon its approval of this Agreement or any part thereof, to relieve MIAX, MIAX PEARL and MIAX Emerald of any and all responsibilities with respect to matters allocated to FINRA pursuant to this Agreement; provided, however, that this Agreement shall not be effective until the Effective Date.

19. *Severability.* Any term or provision of this Agreement that is invalid or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such invalidity or unenforceability without rendering invalid or unenforceable the remaining terms and provisions of this Agreement or affecting the validity or enforceability of any of the terms or provisions of this Agreement in any other jurisdiction.

20. *Counterparts.* This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, and such counterparts together shall constitute one and the same instrument.

Exhibit 1

Miami International Securities Exchange, LLC, MIAX PEARL, LLC and MIAX Emerald, LLC Rules Certification for 17d–2 Agreement With FINRA

Miami International Securities Exchange, LLC (''MIAX''), MIAX PEARL, LLC (''MIAX PEARL'') and MIAX Emerald, LLC (''MIAX Emerald'') hereby certify that the requirements contained in the rules listed below are identical to, or substantially similar to, the comparable FINRA (NASD) Rule, Exchange Act provision or SEC rule identified (''Common Rules'').

MIAX rules	MIAX PEARL rules	MIAX Emerald rules	FINRA (NASD) rules, Exchange Act provision or SEC rule
Rule 301 Just and Equitable Principles of Trade [1].	Rule 301 Just and Equitable Principles of Trade [1].	Rule 301 Just and Equitable Principles of Trade [1].	FINRA Rule 2010 Standards of Commercial Honor and Principles of Trade
Rule 303 Prevention of the Misuse of Material Nonpublic Information [1] [#].	Rule 303 Prevention of the Misuse of Material Nonpublic Information [1] [#].	Rule 303 Prevention of the Misuse of Material Nonpublic Information [1] [#].	Section 15(g) of the Exchange Act and FINRA Rule 3110(b)(1) Supervision
Rule 315 Anti-Money Laundering Compliance Program [#].	Rule 315 Anti-Money Laundering Compliance Program [#].	Rule 315 Anti-Money Laundering Compliance Program [#].	FINRA Rule 3310 Anti-Money Laundering Compliance Program
Rule 318(a) Manipulation	Rule 318(a) Manipulation	Rule 318(a) Manipulation	FINRA Rule 2020 Use of Manipulative, Deceptive or other Fraudulent Devices
Rule 318(b) Manipulation	Rule 318(b) Manipulation	Rule 318(b) Manipulation	FINRA Rule 6140(d) Other Trading Practices
Rule 319 Forwarding of Proxy and Other Issuer-Related Materials.	Rule 319 Forwarding of Proxy and Other Issuer-Related Materials.	Rule 319 Forwarding of Proxy and Other Issuer-Related Materials.	FINRA Rule 2251 Processing and Forwarding of Proxy and Other Issuer-Related Materials
Rule 320 Trading Ahead of Research Reports.	Rule 320 Trading Ahead of Research Reports.	Rule 320 Trading Ahead of Research Reports.	FINRA Rule 5280 Trading Ahead of Research Reports
Rule 800(a), (b) and (d) Maintenance, Retention and Furnishing of Books, Records and Other Information [1] [#].	Rule 800(a), (b) and (d) Maintenance, Retention and Furnishing of Books, Records and Other Information [1] [#].	Rule 800(a), (b) and (d) Maintenance, Retention and Furnishing of Books, Records and Other Information [1] [#].	FINRA Rule 4511 General Requirements * and Section 17 of the Exchange Act and the rules thereunder [#]
Rule 1900 Registration Requirements [#].	Rule 3100 Registration Requirements [#].	Rule 1900 Registration Requirements [#].	FINRA Rule 1210 Registration Requirements; FINRA By-Laws Article V, Sec. 2 Application for Registration; and FINRA By-Laws Article V, Sec. 3 Notification by Member to the Corporation and Association Person of Termination; Amendments to Notification
Rule 1901 Registration Categories [#].	Rule 3101 Registration Categories [#].	Rule 1901 Registration Categories [#].	Rule 1220 Registration Categories [2]
Rule 1902(a), (b)(1)–(4) and Interpretations and Policies .01 Associated Persons Exempt from Registration.	Rule 3102(a), (b)(1)–(4) and Interpretations and Policies .01 Associated Persons Exempt from Registration.	Rule 1902(a), (b)(1)–(4) and Interpretations and Policies .01 Associated Persons Exempt from Registration.	FINRA Rule 1230 Associated Persons Exempt from Registration
Rule 1903 Continuing Education Requirements [#].	Rule 3103 Continuing Education Requirements [#].	Rule 1903 Continuing Education Requirements [#].	FINRA Rule 1240 Continuing Education Requirements
Rule 1321 Transfer of Accounts	Rule 1321 Transfer of Accounts ..	Rule 1321 Transfer of Accounts ..	FINRA Rule 11870 Customer Account Transfer Contracts
Rule 1325 Telemarketing	Rule 1325 Telemarketing	Rule 1325 Telemarketing	FINRA Rule 3230 Telemarketing
	*Rule 2100 Business Conduct of Members **.	....	*FINRA Rule 2010 Standards of Commercial Honor and Principles of Trade **

MIAX rules	MIAX PEARL rules	MIAX Emerald rules	FINRA (NASD) rules, Exchange Act provision or SEC rule
	Rule 2101 Violations Prohibited #*	....	*FINRA Rule 2010 Standards of Commercial Honor* and Principles of Trade and FINRA Rule 3110 Supervision**
	Rule 2102 Use of Fraudulent Devices.*	....	*FINRA Rule 2020 Use of Manipulative, Deceptive or Other Fraudulent Devices**
	Rule 2104 Communications with the Public.	....	*FINRA Rule 2210 Communications with the Public*
	Rule 2105 Know Your Customer	....	*FINRA Rule 2090 Know Your Customer*
	Rule 2106 Fair Dealing with Customers.	....	*FINRA Rule 2020 Use of Manipulative, Deceptive or Other Fraudulent Device*, FINRA Rule 2010 Standards of Commercial Honor and Principles of Trade*, FINRA Rule 2111(a) and SM .06 Suitability, FINRA Rule 2150(a) Improper Use of Customers' Securities or Funds; Prohibition Against Guarantees and Sharing in Accounts, and FINRA Rule 3240(a) Borrowing From or Lending to Customers*
	Rule 2107 Suitability	....	*FINRA Rule 2111*
	Rule 2108(a) The Prompt Receipt and Delivery of Securities.	....	*FINRA Rule 11860 COD Orders*
	Rule 2108(b) The Prompt Receipt and Delivery of Securities.	....	*SEC Regulation SHO*
	Rule 2109 Charges for Services Performed.	....	*FINRA Rule 2122 Charges for Services Performed*
	Rule 2110 Use of Information	....	*FINRA Rule 2060 Use of Information Obtained in Fiduciary Capacity*
	Rule 2111 Publication of Transactions and Quotations #.	....	*FINRA Rule 5210 Publication of Transactions and Quotations*
—	*Rule 2112 Offers at Stated Prices*	....	*FINRA Rule 5220 Offers at Stated Prices*
	Rule 2113 Payments Involving Publications that Influence the Market Price of a Security.	....	*FINRA Rule 5230 Payments Involving Publications that Influence the Market Price of a Security*
	Rule 2114 Customer Confirmations.	....	*FINRA Rule 2232(a) Customer Confirmations and SEC Rule 10b–10 Confirmation of Transactions*
	Rule 2115 Disclosure of Control Relationship with Issuer.	....	*FINRA Rule 2262 Disclosure of Control Relationship With Issuer*
	Rule 2116 Discretionary Accounts	....	*FINRA Rule 3260 Discretionary Accounts*
	Rule 2117 Improper Use of Customers' Securities or Funds; Prohibition Against Guarantees and Sharing in Accounts.	....	*FINRA Rule 2150 Improper Use of Customers' Securities or Funds; Prohibition Against Guarantees and Sharing in Accounts*
	Rule 2118 Influencing or Rewarding Employees of Others.	....	*FINRA Rule 3220 Influencing or Rewarding Employees of Others*
	Rule 2119 Telemarketing	....	*FINRA Rule 3230 Telemarketing*
	Rule 2200 General Requirements #.	....	*Section 17 of the Exchange Act and rules thereunder and FINRA Rule 4511(a) and (c) General Requirements* [3]
	Rule 2201 Customer Account Information.	....	*Rule 4512 Customer Account Information*
	Rule 2203 Record of Written Complaints.	....	*FINRA Rule 4513 Records of Written Customer Complaints*
	Rule 2204 Disclosure of Financial Condition.	....	*FINRA Rule 2261 Disclosure of Financial Condition*
	Rule 2300 Supervision #	....	*FINRA Rule 3110 Supervision**

MIAX rules	MIAX PEARL rules	MIAX Emerald rules	FINRA (NASD) rules, Exchange Act provision or SEC rule
	Rule 2301 Supervisory Control System.	....	*FINRA Rule 3120 Supervisory Control System**
	Rule 2303 Prevention of the Misuse of Material Non-Public Information #.*	....	*Section 15(g) of the Exchange Act* and FINRA Rule 3110(b)(1) Supervision**
	Rule 2304 Anti-Money Laundering Compliance Program[4] #.	....	*FINRA Rule 3310 Anti-Money Laundering Compliance Program*
	Rule 2262(e)(3) & (4) Limit Up-Limit Down Plan and Trading Halts.	....	*FINRA Rule 6190(a) & (b) Compliance with Regulation NMS Plan to Address Extraordinary Market Volatility*
	Rule 2623 Short Sales #	....	*FINRA Rule 6182 Trade Reporting of Short Sales*
	Rule 2700 Market Manipulation ...	....	*FINRA Rule 5210 Publication of Transactions and Quotations, FINRA Rule 2020 Use of Manipulative, Deceptive or Other Fraudulent Devices*, FINRA Rule 2010 Standards of Commercial Honor and Principles of Trade*, and FINRA Rule 6140(a) Other Trading Practices*
	Rule 2701 Fictitious Transactions	....	*FINRA Rule 6140 Other Trading Practices and FINRA Rule 5210 Supplementary Material .02 Self-Trades*
	Rule 2702 Excessive Sales By an Equity Member.	....	*FINRA Rule 6140(c) Other Trading Practices*
	Rule 2703 Manipulative Transactions.	....	*FINRA Rule 6140 Other Trading Practices*
	Rule 2704 Dissemination of False Information.	....	*FINRA Rule 6140(e) Other Trading Practices*
	*Rule 2705 Prohibition Against Trading Ahead of Customer Orders # **.*	....	*FINRA Rule 5320 Prohibition Against Trading Ahead of Customer Orders***
	Rule 2708 Trade Shredding	....	*FINRA Rule 5290 Order Entry and Execution Practices*
	*Rule 2710 Best Execution and Interpositioning**.*	....	*FINRA Rule 5310 Best Execution and Interpositioning***
	*Rule 2712 Trading Ahead of Research Reports**.*	....	*FINRA Rule 5280 Trading Ahead of Research Reports***
	*Rule 2714 Front Running of Block Transactions**.*	....	*FINRA Rule 5270 Front Running of Block Transactions***
	Rule 2802 Forwarding of Proxy and Other Issuer-Related Materials.	....	*FINRA Rule 2251 Processing and Forwarding of Proxy and Other Issuer-Related Materials*

[1] FINRA shall only have Regulatory Responsibilities regarding the rule and not the interpretations and policies.

Common Rules shall not include any provisions regarding (i) notice, reporting or any other filings made directly to or from MIAX, MIAX PEARL or MIAX Emerald, (ii) incorporation by reference of *other* MIAX, MIAX PEARL or MIAX Emerald Rules that are not Common Rules, (iii) exercise of discretion in a manner that differs from FINRA's exercise of discretion including, but not limited to exercise of exemptive authority by MIAX, MIAX PEARL or MIAX Emerald, (iv) prior written approval of MIAX, MIAX PEARL or MIAX Emerald and (v) payment of fees or fines to MIAX, MIAX PEARL or MIAX Emerald.

* *FINRA shall not have any Regulatory Responsibilities for these rules as they pertain to violations of insider trading activities, which is covered by a separate 17d–2 Agreement by and among Cboe BZX Exchange, Inc., Cboe BYX Exchange, Inc., Chicago Stock Exchange, Inc., Cboe EDGA Exchange Inc., Cboe EDGX Exchange Inc., Financial Industry Regulatory Authority, Inc., MEMX, LLC, Nasdaq BX, Inc., Nasdaq PHLX LLC, The Nasdaq Stock Market LLC, NYSE National, Inc., New York Stock Exchange, LLC, NYSE American LLC, NYSE Arca Inc., and Investors' Exchange LLC and the Long-Term Stock Exchange, Inc. effective May 26, 2020, as may be amended from time to time.*

[2] FINRA shall only have Regulatory Responsibilities regarding MIAX and MIAX Emerald Rules 1901 or MIAX Pearl Rule 3101 to the extent that MIAX, MIAX Pearl or MIAX Emerald recognize the same categories of principal and representative registration.

[3] FINRA shall not have Regulatory Responsibilities regarding requirements to keep records "in conformity with . . . Exchange Rules;" responsibility for such requirement remains with MIAX PEARL.

[4] FINRA shall only have Regulatory Responsibilities regarding the rule and not the interpretations and policies.

** FINRA shall perform the surveillance responsibilities for the double star rules for MIAX PEARL Equities. These rules may be cited by FINRA in both the context of this Agreement and the Regulatory Services Agreement.

In addition, the following provisions shall be part of this 17d–2 Agreement:

- SEA Rule 200 of Regulation SHO—Definition of Short Sales and Marking Requirements **
- SEA Rule 201 of Regulation SHO—Circuit Breaker **

- SEA Rule 203 of Regulation SHO—Borrowing and Delivery Requirements **
- SEA Rule 204 of Regulation SHO—Close-Out Requirement **
- *SEA Rule 101 of Regulation M—Activities by Distribution Participants* **
- *SEA Rule 102 of Regulation M—Activities by Issuers and Selling Security Holders During a Distribution* **
- *SEA Rule 103 of Regulation M—Nasdaq Passive Market Making* **
- *SEA Rule 104 of Regulation M—Stabilizing and Other Activities in Connection with an Offering* **
- *SEA Rule 105 of Regulation M—Short Selling in Connection With a Public Offering* **
- *SEA Rule 604 of Regulation NMS—Display of Customer Limit Orders* **
- *SEA Rule 606 of Regulation NMS—Disclosure of Routing Information* **
- *SEA Rule 610(d) of Regulation NMS—Locking or Crossing Quotations* **
- *SEA Rule 611 of Regulation NMS—Order Protection Rule* **
- *SEA Rule 10b–5 Employment of Manipulative and Deceptive Devices* *
- *SEA Rule 17a–3/17a–4—Records to Be Made by Certain Exchange Members, Brokers, and Dealers/Records to Be Preserved by Certain Exchange Members, Brokers, and Dealers* *
- SEA Rule 14e–4—Prohibited Transactions in Connection with Partial Tender Offers ^

^ FINRA shall perform surveillance[, investigation, and Enforcement Responsibilities] for SEA Rule 14e–4(a)(1)(ii)(D).

** FINRA shall not have any Regulatory Responsibilities for these rules as they pertain to violations of insider trading activities, which is covered by a separate 17d–2 Agreement by and among Cboe BZX Exchange, Inc., Cboe BYX Exchange, Inc., Chicago Stock Exchange, Inc., Cboe EDGA Exchange Inc., Cboe EDGX Exchange Inc., Financial Industry Regulatory Authority, Inc., MEMX, LLC, Nasdaq BX, Inc., Nasdaq PHLX LLC, The Nasdaq Stock Market LLC, NYSE National, Inc., New York Stock Exchange, LLC, NYSE American LLC, NYSE Arca Inc., and Investors' Exchange LLC and the Long-Term Stock Exchange, Inc. effective May 26, 2020, as may be amended from time to time.*

*** FINRA shall perform the surveillance responsibilities for the double star rules for MIAX PEARL Equities. These rules may be cited by FINRA in both the context of this Agreement and the Regulatory Services Agreement.*

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. 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 4–678 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 4–678. 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 plan that are filed with the Commission, and all written communications relating to the proposed plan 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 plan also will be available for inspection and copying at the principal offices of FINRA, MIAX, MIAX PEARL, and MIAX Emerald. 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 4–678 and should be submitted on or before October 5, 2020.

V. Discussion

The Commission finds that the proposed Amended Plan is consistent with the factors set forth in Section 17(d) of the Act [15] and Rule 17d–2(c) thereunder [16] in that the proposed Amended Plan is necessary or appropriate in the public interest and for the protection of investors, fosters cooperation and coordination among SROs, and removes impediments to and fosters the development of the national market system. In particular, the Commission believes that the proposed Amended Plan should reduce unnecessary regulatory duplication by allocating to FINRA certain examination and enforcement responsibilities for Common Members that would otherwise be performed by FINRA and at least one of MIAX, MIAX PEARL, or MIAX Emerald. Accordingly, the proposed Amended Plan promotes efficiency by reducing costs to common members. Furthermore, because MIAX, MIAX PEARL, MIAX Emerald and FINRA will coordinate their regulatory functions in accordance with the Amended Plan, the Amended Plan should promote investor protection.

The Commission notes that, under the Amended Plan, MIAX, MIAX PEARL, MIAX Emerald, and FINRA have allocated regulatory responsibility for those MIAX, MIAX PEARL, and MIAX Emerald rules, set forth in the Certification, that are substantially similar to the applicable FINRA rules in that examination for compliance with such provisions and rules would not require FINRA to develop one or more new examination standards, modules, procedures, or criteria in order to analyze the application of the rule, or a common member's activity, conduct, or output in relation to such rule. In addition, under the Amended Plan, FINRA would assume regulatory responsibility for certain provisions of the federal securities laws and the rules and regulations thereunder that are set forth in the Certification. The common rules covered by the Amended Plan are specifically listed in the Certification, as may be amended by the parties from time to time.

According to the Amended Plan, MIAX, MIAX PEARL, and MIAX Emerald will review the Certification at least annually, or more frequently if required by changes in either the rules of MIAX, MIAX PEARL, MIAX Emerald, or FINRA, and, if necessary, submit to FINRA an updated list of common rules to add MIAX, MIAX PEARL, or MIAX Emerald rules not included on the then-current list of common rules that are substantially similar to FINRA rules; delete MIAX, MIAX PEARL, or MIAX Emerald rules included in the then-current list of common rules that no longer qualify as common rules; and confirm that the remaining rules on the list of common rules continue to be MIAX, MIAX PEARL, or MIAX Emerald

[15] 15 U.S.C. 78q(d).

[16] 17 CFR 240.17d–2(c).

rules that qualify as common rules.[17] FINRA will then confirm in writing whether the rules listed in any updated list are common rules as defined in the Amended Plan. Under the Amended Plan, MIAX, MIAX PEARL, and MIAX Emerald also will provide FINRA with a current list of common members and shall update the list no less frequently than once each quarter.[18] The Commission believes that these provisions are designed to provide for continuing communication between the parties to ensure the continued accuracy of the scope of the proposed allocation of regulatory responsibility.

The Commission is hereby declaring effective an Amended Plan that, among other things, allocates regulatory responsibility to FINRA for the oversight and enforcement of all MIAX, MIAX PEARL, and MIAX Emerald rules that are substantially similar to the rules of FINRA for common members of FINRA and MIAX, FINRA and MIAX PEARL, and FINRA and MIAX Emerald. Therefore, modifications to the Certification need not be filed with the Commission as an amendment to the Amended Plan, provided that the parties are only adding to, deleting from, or confirming changes to MIAX, MIAX PEARL, or MIAX Emerald rules in the Certification in conformance with the definition of common rules provided in the Amended Plan. However, should the parties decide to add a MIAX, MIAX PEARL, or MIAX Emerald rule to the Certification that is not substantially similar to a FINRA rule; delete a MIAX, MIAX PEARL, or MIAX Emerald rule from the Certification that is substantially similar to a FINRA rule; or leave on the Certification a MIAX, MIAX PEARL, or MIAX Emerald rule that is no longer substantially similar to a FINRA rule, then such a change would constitute an amendment to the Amended Plan, which must be filed with the Commission pursuant to Rule 17d–2 under the Act.[19]

Under paragraph (c) of Rule 17d–2, the Commission may, after appropriate notice and comment, declare a plan, or any part of a plan, effective. In this instance, the Commission believes that appropriate notice and comment can take place after the proposed amendment is effective. In particular, the purpose of the amendment is to add MIAX PEARL equities rules and certain federal securities laws to the Certification. The Commission notes that the most recent prior amendment to the Plan was published for comment and the Commission did not receive any comments thereon.[20] The Commission believes that the current amendment to the Plan does not raise any new regulatory issues that the Commission has not previously considered, and therefore believes that the amended Plan should become effective without any undue delay.

VI. Conclusion

This order gives effect to the Amended Plan filed with the Commission in File No. 4–678. The parties shall notify all members affected by the Amended Plan of their rights and obligations under the Amended Plan.

It is therefore ordered, pursuant to Section 17(d) of the Act, that the Amended Plan in File No. 4–678, between the FINRA, MIAX, MIAX PEARL, and MIAX Emerald, filed pursuant to Rule 17d–2 under the Act, hereby is approved and declared effective.

It is further ordered that MIAX, MIAX PEARL, and MIAX Emerald are each relieved of those responsibilities allocated to FINRA under the Amended Plan in File No. 4–678.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[21]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20132 Filed 9–11–20; 8:45 am]

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[17] *See* paragraph 2 of the Amended Plan.

[18] *See* paragraph 3 of the Amended Plan.

[19] The addition to or deletion from the Certification of any federal securities laws, rules, and regulations for which FINRA would bear responsibility under the Amended Plan for examining, and enforcing compliance by, common members, also would constitute an amendment to the Amended Plan.

[20] *See* Securities Exchange Act Release No. 85189 (February 25, 2019), 84 FR 7153 (March 1, 2019).

[21] 17 CFR 200.30–3(a)(34).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89787; File No. SR–NYSEArca–2020–78]

Self-Regulatory Organizations; NYSE Arca, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Modify the NYSE Arca Options Fee Schedule

September 8, 2020.

Pursuant to Section 19(b)(1)[1] of the Securities Exchange Act of 1934 (the ''Act'')[2] and Rule 19b–4 thereunder,[3] notice is hereby given that, on September 1, 2020, NYSE Arca, Inc. (''NYSE Arca'' or the ''Exchange'') filed with the Securities and Exchange Commission (the ''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 modify the NYSE Arca Options Fee Schedule (''Fee Schedule'') regarding pricing incentives for certain posted volume. The Exchange proposes to implement the fee change effective September 1, 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 the Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of this filing is to amend the Fee Schedule regarding pricing incentives for certain posted volume. In particular, the Exchange proposes to adopt a new Customer Posting Tier for non-Penny Issues and to implement a cap on the maximum per contract credit for Professional Customer executions. The Exchange proposes to implement the fee change effective September 1, 2020.

The Exchange has established various pricing incentives—or posting credit tiers—designed to encourage OTP Holders and OTP Firms (collectively, ''OTP Holders'') to direct additional order flow to the Exchange to achieve more favorable pricing and higher credits. Currently, the Fee Schedule provides separate pricing programs for

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

executed Customer posted interest in Penny issues and non-Penny issues—namely Customer Posting Credit Tiers in Penny Issues and Customer Posting Credit Tiers in non-Penny Issues (collectively, the ''Customer Posting Tiers''). As such, OTP Holders receive a base per contract credit for executions of Customer posted interest, which credit increases if certain volume criteria and thresholds are met. OTP Holders may also qualify for the Customer Incentive Program, which offers one of five ways to earn an additional credit (to the Customer Posting Tiers) if certain volume criteria and thresholds are met. The Exchange notes that for purposes of these pricing programs, Professional Customer interest is currently treated the same as Customer interest.[4]

The Exchange proposes two changes to the current pricing incentives: To adopt a new Customer Posting Tier for non-Penny Issues (the ''Non-Penny Posting Tiers'') and to implement a cap on the maximum per contract credit for Professional Customer executions regardless of whether an OTP Holders qualifies for higher credits per the pricing incentive programs, which are described in more detail below.

New Tier E to the Non-Penny Posting Tiers

The Non-Penny Posting Tiers consist of a base tier per contract credit of ($0.75) on executions of Customer posted interest in non-Penny issues as five other tiers—Tiers A–E, which offer increased credits, ranging from ($0.85) to ($1.02), based on meeting increased posted volume requirements. The Exchange proposes to modify the Fee Schedule to add a new Tier E, and to rename current Tier E as Tier F.[5] New Tier E would provide a ($1.01) per contract credit provided an OTP Holder executes at least 1.50% of Total Industry Customer equity and ETF option average daily volume (''TCADV'') from Customer posted interest in all issues.[6]

Proposed Cap on Available Credit for Professional Customer Volume

The Exchange also proposes to modify the Customer Posting Tiers and the Customer Incentive Program, which programs currently treat Professional Customer interest the same as Customer interest, by placing a limit or cap on the maximum available per contract credit on Professional Customer posted interest.[7]

Specifically, as proposed, the maximum per-contract credit for Professional Customer posted interest would be ($0.49) and ($1.00) in Penny and non-Penny issues, respectively.[8] The proposed per-contract credit limits on Professional Customer posted volume would apply regardless of which Customer Posting Credit Tier an OTP Holder achieves or whether an OTP Holder qualified for an additional credit per the Customer Incentive Program. This proposed change would impact OTP Holders with Professional Customer order flow that have achieved the highest Customer Posting Tiers. Specifically, OTP Holders with Professional Customer order flow that would be impacted by the proposed change includes those that achieve Tier 6 of the Customer Posting Tiers in Penny issues, proposed new Tiers E and F of the Customer Posting Tiers in non-Penny issues, and OTP Holders that qualify for an additional credit per the Customer Incentive Program, if those OTP Holders qualified for Tier 5 or 6 of the Customer Posting Tiers in Penny issues or Tiers E–D of the Customer Posting Tiers in non-Penny issues. Despite capping the per-contract credit on Professional Customers, the Exchange believes that the existing Customer Posting Tiers and Customer Incentive Program would continue to attract order flow, including Professional Customer volume.

The Exchange cannot predict with certainty whether any OTP Holders will avail themselves of new Tier E to the Non-Penny Posting Tiers or be impacted by the proposed limit on per-contract credits for Professional Customer volume under the Customer Posting Tiers or Customer Incentive Program.

2.Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[9] in general, and furthers the objectives of Sections 6(b)(4) and (5) of the Act,[10] 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.''[11]

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.[12] Therefore, currently no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in June 2020, the Exchange had slightly over 10% market share of executed volume of multiply-listed equity & ETF options trades.[13]

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 and rebates can have a direct effect on the ability of an exchange to compete for order flow.

The Exchange believes that proposed new Tier E to the Non-Penny Posting Tiers is reasonable as it is designed to incentivize OTP Holders to (continue to) direct order flow, particularly Customer flow, to the Exchange. An increase in Customer volume would create more

[4] *See* Fee Schedule, NYSE Arca OPTIONS: TRADE–RELATED CHARGES FOR STANDARD OPTIONS, Preamble (providing that ''[u]nless Professional Customer executions are specifically delineated, such executions will be treated as 'Customer' executions for fee/credit purposes'').

[5] *See* proposed Fee Schedule, Customer Posting Tier for non-Penny Issues.

[6] *See* Fee Schedule, Endnote 8 (providing that TCADV includes OCC calculated Customer volume of all types, including Complex Order Transactions and QCC transactions, in equity and ETF options).

[7] *See* proposed Fee Schedule, Endnote 16. *See also* Customer Posting Credit Tiers in Penny Issues, Customer Posting Credit Tiers in non-Penny Issues and Customer Incentive Program (referencing new Endnote 16).

[8] *See supra* note 4 (regarding Professional Customer executions being treated as 'Customer' executions for fee/credit purposes, unless otherwise specified in the Fee Schedule).

[9] 15 U.S.C. 78f(b).

[10] 15 U.S.C. 78f(b)(4) and (5).

[11] *See* Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37499 (June 29, 2005) (S7–10–04) (''Reg NMS Adopting Release'').

[12] 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.*

[13] Based on OCC data, *see id.,* the Exchange's market share in equity-based options was 9.59% for the month of June 2019 and 10.69% for the month of June 2020.

trading opportunities, which, in turn attracts Market-Makers. A resulting increase in Market-Maker activity may facilitate tighter spreads, which may lead to an additional increase of order flow from other market participants, further contributing to a deeper, more liquid market to the benefit of all market participants by creating a more robust and well-balanced market ecosystem. In addition, to the extent that proposed new Tier E attracts more Customer posted interest in non-Penny issues to the Exchange, this increased order flow would continue to make the Exchange a more competitive venue for order execution, which, in turn, promotes just and equitable principles of trade and removes impediments to and perfects the mechanism of a free and open market and a national market system.

The Exchange believes the proposed limit on per contract credit for Professional Customer volume is reasonable as it is consistent with pricing on other options exchanges that likewise offer higher credits/rebates for Customer volume other than Professional Customer volume.[14] In addition, the Exchange believes it is reasonable to continue to offer the highest rebates for Customer volume. Customer volume offers unique benefits to the market by providing more trading opportunities, which attracts market makers to the benefit of all market participants. An increase in the activity of these market participants in turn facilitates tighter spreads, which may cause an additional corresponding increase in order flow from other market participants. Customer volume is the most sought after liquidity among OTP Holders. With respect to Professional Customers, the Exchange believes that its Customer Posting Tiers and Customer Incentive Program would continue to encourage OTP Holders to post Professional Customer volume to the Exchange despite the new cap on per contract credit, which increased liquidity would promote market depth, price discovery and improvement and enhance order execution opportunities for market participants.

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 OTP Holders are not obligated to try to achieve new Tier E. Moreover, the proposal is designed to incent OTP Holders to aggregate all Customer posting interest at the Exchange as a primary execution venue. To the extent that the proposed change attracts more Customer posting interest to the Exchange, this 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 Customer posting credits because the proposed modification would be available to all similarly-situated market participants on an equal and non-discriminatory basis.

The proposal is based on the amount and type of business transacted on the Exchange and OTP Holders are not obligated to try to achieve new Tier E, nor are they obligated to execute posted interest, particularly Professional Customer interest. Rather, the proposal is designed to encourage OTP Holders to utilize the Exchange as a primary trading venue for Customer posted interest (if they have not done so previously) or increase volume sent to the Exchange. To the extent that the proposed change attracts more Customer interest, including posted interest, to the Exchange, this 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 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.

Regarding the proposed limit of the per contract credit on Professional Customer volume, the Exchange notes that is equitable and not unfairly discriminatory to cap incentives for Professional Customers who, unlike Customers, have access to sophisticated trading systems that contain functionality not available to retail Customers, including continuously updated pricing models based on real-time streaming data, access to multiple markets simultaneously, and order and risk management tools. As such, the Exchange believes placing a cap on the credits available to Professional Customers (while imposing no such cap on Customer flow) is not unfairly discriminatory to these sophisticated actors.

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.'' [15]

Intramarket Competition. The proposed new Tier E as well as the cap on available credit for Professional Customer volume is designed to (continue to) attract additional order flow (particularly Customer posted interest) to the Exchange. Customer volume offers unique benefits to the market which benefits all market participants. Customer volume benefits all market participants by providing more trading opportunities, which attracts market makers. An increase in the activity of these market participants in turn facilitates tighter spreads, which may cause an additional corresponding

[14] *See e.g.,* NASDAQ Options Market LLC (''NOM'') Pricing Schedule, Options 7, Section 2, Nasdaq Options Market Fees and Rebates (paying Professionals a $0.48 per contract Rebate to Add Liquidity in Penny Symbols whereas Customers are paid $0.50 per contract; paying Professionals a $0.90 per contract Rebate to Add Liquidity in Non-Penny Symbols whereas Customers are paid $1.00 per contract).

[15] *See* Reg NMS Adopting Release, *supra* note 11, at 37499.

increase in order flow from other market participants. The Exchange believes that the credits available via the Customer Posting Tiers and the Customer Incentive Program—despite the proposed credit cap on Professional Customer volume—would continue to encourage OTP Holders to direct their Professional Customer order flow to the Exchange, as the proposed limit is competitive with rates offers on other options exchanges.[16] Moreover, the Exchange notes that Professional Customers, unlike Customers, have access to sophisticated trading systems that contain functionality not available to Customers and therefore the proposed disparate treatment of Professional Customer volume would not pose an undue burden on competition.

Intermarket Competition. The Exchange operates in a highly competitive market in which market participants can readily favor one of the 16 competing option exchanges if they deem fee levels at a particular venue to be excessive. In such an environment, the Exchange must continually adjust its fees to remain competitive with other exchanges and to attract order flow to the Exchange. 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.[17] Therefore, currently no exchange possesses significant pricing power in the execution of multiply-listed equity & ETF options order flow. More specifically, in January 2020, the Exchange had slightly more than 10% market share of executed volume of multiply-listed equity & ETF options trades.[18]

The Exchange believes that the proposed rule change reflects this competitive environment because it modifies the Exchange's fees in a manner designed to incent OTP Holders to (continue to) direct trading interest (particularly Customer posted interest) to the Exchange, to provide liquidity and to attract order flow. To the extent that this purpose is achieved, all the Exchange's market participants should benefit from the improved market quality and increased opportunities for price improvement.

The Exchange believes that the proposed change could promote competition between the Exchange and other execution venues, including those that currently offer similar Customer posting credits, by encouraging additional orders to be sent to the Exchange for execution. The Exchange also believes that the proposed change is designed to provide the public and investors with a Fee Schedule that is clear and consistent, thereby reducing burdens on the marketplace and facilitating investor protection.

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) [19] of the Act and subparagraph (f)(2) of Rule 19b–4 [20] 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) [21] 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–2020–78 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–2020–78. 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–NYSEArca–2020–78 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[22]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20131 Filed 9–11–20; 8:45 am]

BILLING CODE 8011–01–P

[16] *See supra* note 14.

[17] 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.*

[18] Based on OCC data, *see id.,* the Exchange's market share in equity-based options was 9.59% for the month of June 2019 and 10.69% for the month of June 2020.

[19] 15 U.S.C. 78s(b)(3)(A).

[20] 17 CFR 240.19b–4(f)(2).

[21] 15 U.S.C. 78s(b)(2)(B).

[22] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89776; File No. SR–CboeEDGA–2020–025]

Self-Regulatory Organizations; Cboe EDGA Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Update Rule 13.4(a), Stating It Will Utilize MIAX PEARL Market Data From the CQSUQDF for Purposes of Order Handling, Routing, Execution, and Related Compliance Processes

September 8, 2020.

Pursuant to Section 19(b)(1) [1] of the Securities Exchange Act of 1934 (the ''Act'') [2] and Rule 19b–4 thereunder,[3] notice is hereby given that on August 25, 2020, Cboe EDGA Exchange, Inc. (the ''Exchange'' or ''EDGA'') filed with the Securities and Exchange Commission (the ''Commission'') the proposed rule change as described in Items I and II 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

Cboe EDGA Exchange, Inc. (''EDGA'' or the ''Exchange'') proposes a rule change to Rule 13.4(a), stating it will utilize MIAX PEARL market data from the CQSUQDF for purposes of order handling, routing, execution, and related compliance processes. The text of the proposed rule change is provided in Exhibit 5.

The text of the proposed rule change is also available on the Exchange's website (*http://markets.cboe.com/us/equities/regulation/rule_filings/edga/*), at the Exchange's Office of the Secretary, 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to update Rule 13.4(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of the MIAX PEARL as an equities exchange.

On August 14, 2020, the Commission approved MIAX PEARL's proposed rule change to establish rules governing the trading of equities securities.[4] MIAX PEARL announced that it plans to launch equities trading on September 25, 2020.[5] The Exchange, therefore, proposes to update Rule 13.4(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of MIAX PEARL as an equities exchange beginning on September 25, 2020. Specifically, the Exchange proposes to amend Rule 13.4(a) to include MIAX PEARL by stating it will utilize MIAX PEARL market data from the Consolidated Quotation System (''CQS'')/UTP Quotation Data Feed (''UQDF'') for purposes of order handling, routing, execution, and related compliance processes. At this stage, no secondary source for MIAX PEARL market data will be used.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[6] in general, and furthers the objectives of Section 6(b)(5) of the Act,[7] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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.

The Exchange believes that its proposal to update Exchange Rule 13.4(a) to include MIAX PEARL will ensure that the Rule correctly identifies and publicly states on a market-by-market basis all of the specific network processor and proprietary data feeds that the Exchange utilizes for the handling, routing, and execution of orders, and for performing the regulatory compliance checks related to each of those functions. The proposed rule changes also remove impediments to and perfects the mechanism of a free and open market and protects investors and the public interest because it provides additional specificity, clarity and transparency.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange believes its proposed rule change would not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. To the contrary, the Exchange believes the proposal would enhance competition because including all of the exchanges enhances transparency and enables investors to better assess the quality of the Exchange's execution and routing services.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from Members or other interested parties.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

(i) Significantly affect the protection of investors or the public interest;

(ii) impose any significant burden on competition; and

(iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act [8] and Rule 19b–4(f)(6) thereunder.[9]

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

[4] *See* Securities Exchange Act No. 89562 (August 14, 2020).

[5] *See supra* note 3 [sic].

[6] 15 U.S.C. 78f.

[7] 15 U.S.C. 78f(b)(5).

[8] 15 U.S.C. 78s(b)(3)(A).

[9] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change,

Continued

At any time within 60 days of the filing of the 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.

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–CboeEDGA–2020–025 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–CboeEDGA–2020–025. 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–CboeEDGA–2020–025 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[10]

J. Matthew DeLesDernier,

Assistant Secretary.

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at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has fulfilled this requirement.

[10] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

Sunshine Act Meetings

TIME AND DATE: 2:00 p.m. on Wednesday, September 16, 2020.

PLACE: The meeting will be held via remote means and/or 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 matter of the closed meeting will consist of the following topic:

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: September 9, 2020.

Vanessa A. Countryman,

Secretary.

[FR Doc. 2020–20271 Filed 9–10–20; 11:15 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89789; File No. SR–CBOE–2020–081]

Self-Regulatory Organizations; Cboe Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Amend Rule 5.24

September 8, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the ''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on August 31, 2020, Cboe Exchange, Inc. (the ''Exchange'' or ''Cboe Options'') filed with the Securities and Exchange Commission (the ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Exchange filed the proposal as a ''non-controversial'' proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act[3] and Rule 19b–4(f)(6) thereunder.[4] 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

Cboe Exchange, Inc. (the ''Exchange'' or ''Cboe Options'') proposes to amend Rule 5.24. The text of the proposed rule change is provided below.

(additions are *italicized;* deletions are [bracketed])

* * * * *

Rules of Cboe Exchange, Inc.

* * * * *

Rule 5.24. Disaster Recovery

(a)—(d) No change.

(e) *Loss of Trading Floor.* If the Exchange trading floor becomes

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] 15 U.S.C. 78s(b)(3)(A)(iii).

[4] 17 CFR 240.19b–4(f)(6).

inoperable, the Exchange will continue to operate in a screen-based only environment using a floorless configuration of the System that is operational while the trading floor facility is inoperable. The Exchange will operate using this configuration only until the Exchange's trading floor facility is operational. Open outcry trading will not be available in the event the trading floor becomes inoperable, except in accordance with paragraph (2) below and pursuant to Rule 5.26, as applicable.

(1) *Applicable Rules.* In the event that the trading floor becomes inoperable, trading will be conducted pursuant to all applicable System Rules, except that open outcry Rules will not be in force, including but not limited to the Rules (or applicable portions of the Rules) in Chapter 5, Section G, and as follows (subparagraphs (A) through (E) will be effective until [August 31]N *September 30,* 2020):

* * * * *

The text of the proposed rule change is also available on the Exchange's website (*http://www.cboe.com/AboutCBOE/CBOELegalRegulatoryHome.aspx*), at the Exchange's Office of the Secretary, 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to amend Rule 5.24 regarding the Exchange's business continuity and disaster recovery plans. Rule 5.24 describes which Trading Permit Holders (''TPHs'') are required to connect to the Exchange's backup systems as well as certain actions the Exchange may take as part of its business continuity plans so that it may maintain fair and orderly markets if unusual circumstances occurred that could impact the Exchange's ability to conduct business. This includes what actions the Exchange would take if its trading floor became inoperable. Specifically, Rule 5.24(e) states if the Exchange trading floor becomes inoperable, the Exchange will continue to operate in a screen-based only environment using a floorless configuration of the System that is operational while the trading floor facility is inoperable. The Exchange would operate using that configuration only until the Exchange's trading floor facility became operational. Open outcry trading would not be available in the event the trading floor becomes inoperable.[5]

Rule 5.24(e)(1) currently states in the event that the trading floor becomes inoperable, trading will be conducted pursuant to all applicable System Rules, except that open outcry Rules would not be in force, including but not limited to the Rules (or applicable portions) in Chapter 5, Section G,[6] and that all non-trading rules of the Exchange would continue to apply. The Exchange recently adopted several rule changes that would apply during a time in which the trading floor in inoperable, which are effective until August 31, 2020.[7] The Exchange believes these rules were necessary to implement to maintain a fair and orderly market while the trading floor was not operable in order to create an all-electronic trading environment similar to the otherwise unavailable open outcry trading environment.

As of March 16, 2020, the Exchange suspended open outcry trading to help prevent the spread of COVID–19.[8] The trading floor remained closed until June 15, 2020. During the time when the trading floor was closed, the Exchange operated in an all-electronic trading environment and the temporary rules in Rule 5.24(e)(1) applied to that electronic trading environment. The Exchange believes that, while those temporary rules did not fully replicate open outcry trading, they allowed all-electronic trading to occur more similarly to open outcry trading.[9]

The trading floor is currently open for open outcry trading, and the Exchange is operating pursuant to its normal hybrid trading rules. The Exchange implemented numerous health and safety measures in connection with the reopening of the trading floor on June 15, 2020 to help protect the safety and welfare of the trading floor community and help prevent the continued spread of COVID–19.[10] However, the Exchange recognizes the ongoing nature of the COVID–19 pandemic in the United States, which may cause the Exchange to once again close its trading floor.

In the event the Exchange did close its trading floor again, the Exchange believes it would be necessary to again apply the recently adopted temporary rules in Rule 5.24(e)(1) to maintain a fair and orderly market while the trading floor was not operable in order to create

[5] Pursuant to Rule 5.26, the Exchange may enter into a back-up trading arrangement with another exchange, which could allow the Exchange to use the facilities of a back-up exchange to conduct trading of certain of its products. The Exchange currently has no back-up trading arrangement in place with another exchange.

[6] Chapter 5, Section G of the Exchange's rulebook sets forth the rules and procedures for manual order handling and open outcry trading on the Exchange.

[7] *See* Securities Exchange Act Release Nos. 88386 (March 13, 2020), 85 FR 15823 (March 19, 2020) (SR–CBOE–2020–019); 88447 (March 20, 2020), 85 FR 17129 (March 26, 2020) (SR–CBOE–2020–023); 88490 (March 26, 2020), 85 FR 18318 (April 1, 2020) (SR–CBOE–2020–026); 88530 (March 31, 2020), 85 FR 19182 (April 6, 2020) (SR–CBOE–2020–031); 88886 (May 15, 2020), 85 FR 31008 (May 21, 2020) (SR–CBOE–2020–047); and 89307 (July 14, 2020), 85 FR 43938 (July 20, 2020) (SR–CBOE–2020–066).

[8] On March 11, 2020, the World Health Organization characterized COVID–19 as a pandemic and to slow the spread of the disease, federal and state officials implemented social-distancing measures, placed significant limitations on large gatherings, limited travel, and closed non-essential businesses.

[9] The Exchange continues to consider other enhancements to the all-electronic trading configuration that it believes may permit this configuration to further replicate the open outcry trading environment. The Exchange would submit separate rule filings for any such proposed enhancements. The Exchange notes it recently submitted a separate rule filing to adopt a virtual trading floor, which the Exchange may determine to make available if the trading floor becomes inoperable. *See* Securities Exchange Act Release No. 89131 (June 23, 2020), 85 FR 38951 (June 29, 2020) (SR–CBOE–2020–055). If the Commission approves that filing, and the trading floor subsequently becomes inoperable and the Exchange makes the virtual trading floor available, the temporary rules in Rule 5.24(e)(1) would not be in effect (the Exchange submitted partial Amendment No. 1 to SR–CBOE–2020–055 to make that clear). Separately, the Exchange believes the temporary rules in Rule 5.24(e)(1) should be effective for a period of time while the virtual trading floor is available, the Exchange will submit a separately rule filing to propose that change.

[10] *See* Exchange Notice C2020052601, *Standards of Conduct related to the Reopening of the Cboe Options Trading Floor and COVID–19* (May 26, 2020), *available at https://cdn.cboe.com/resources/release_notes/2020/Standards-of-Conduct-related-to-the-Reopening-of-the-Cboe-Options-Trading-Floor-Notice-Final.pdf.*

an all-electronic trading environment similar to the otherwise unavailable open outcry trading environment. As noted above, Rule 5.24(e)(1) is effective only until August 31, 2020 (and the rules became inapplicable upon the reopening of the trading floor on June 15, 2020). Given the Exchange may believe it is appropriate to close the trading floor with little advanced notice and in a short timeframe to help protect the safety and welfare of the trading floor community, the Exchange proposes to extend the effectiveness of the temporary rules in Rule 5.24(e)(1) to September 30, 2020 (unless further extended). The Exchange believes this will permit the Exchange to as seamlessly as possible transition back to an all-electronic trading environment. The Exchange notes Rule 5.24(e)(1) will not apply to trading during times when the trading floor remains operable.

Previously when the temporary provisions of Rule 5.24(e)(1) were in place, the Exchange's Regulatory Division has continued its standard routine surveillance reviews for electronic trading and implemented a regulatory plan to surveil the rules in place in Rule 5.24(e)(1) when operating in a screen-based only environment. In the event the Exchange closes its trading floor again and the temporary provisions in Rule 5.24(e)(1) become applicable in an all-electronic trading environment, the Exchange's Regulatory Division would reimplement that regulatory plan to surveil those rules.

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with the Securities Exchange Act of 1934 (the ''Act'') and the rules and regulations thereunder applicable to the Exchange and, in particular, the requirements of Section 6(b) of the Act.[11] Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5) [12] requirements that the rules of an exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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. Additionally, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5) [13] requirement that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

In particular, the Exchange believes the proposed rule change will remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, protect investors and the public interest by permitting the Exchange to as seamlessly as possible transition back to an all-electronic trading environment in the event the Exchange determines it is appropriate to again close its trading floor. The Exchange expects it would take this action if it believes necessary and appropriate to help protect the safety and welfare of the trading community. Such a determination may occur with little advance notice, and closure of the trading floor may need to occur in a short time frame. The Exchange continues to believe the recent amendments to Rule 5.24(e)(1) allowed all-electronic trading to occur more similarly to open outcry trading while the trading floor was closed. The Exchange believes the proposed rule change is necessary and appropriate to provide TPHs with execution opportunities in an all-electronic trading environment for orders that generally execute in open outcry trading. Additionally, the proposed rule change will provide TPHs with an all-electronic trading environment to which they became accustomed when the trading floor was previously closed, and therefore will provide investors with consistent rules that apply when the Exchange operates in an all-electronic environment. The proposed rule change will provide investors with definitive knowledge of what rules will apply when the trading floor is closed.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change is not intended as a competitive filing, but rather extends the effectiveness of temporary rules as part of the Exchange's business continuity plans, which are intended to allow the Exchange to continue to maintain fair and orderly markets while the Exchange's trading floor continues to be inoperable.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange neither solicited nor received comments on the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act [14] and Rule 19b–4(f)(6) thereunder.[15]

A proposed rule change filed pursuant to Rule 19b–4(f)(6) under the Act [16] normally does not become operative for 30 days after the date of its filing. However, Rule 19b–4(f)(6)(iii) [17] permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay so that the proposed rule change may become operative immediately. The Exchange believes extension of the temporary rules put in place due to the ongoing COVID–19 pandemic will permit the Exchange to minimize disruptions in the market during a transition back to an all-electronic trading environment if the Exchange believes it is necessary and appropriate to help protect the safety and welfare of the trading community. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest as it will allow the temporary rules to continue with minimal interruption, thereby avoiding investor confusion that could result from an interruption in the effectiveness of the rules. Accordingly, the Commission hereby waives the operative delay and designates the

[11] 15 U.S.C. 78f(b).

[12] 15 U.S.C. 78f(b)(5).

[13] *Id.*

[14] 15 U.S.C. 78s(b)(3)(A).

[15] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Commission has waived the five business day notification requirement for this proposed rule change.

[16] 17 CFR 240.19b–4(f)(6).

[17] 17 CFR 240.19b–4(f)(6)(iii).

proposed rule change operative upon filing.[18]

At any time within 60 days of the filing of the 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 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–CBOE–2020–081 on the subject line.

Paper Comment:

• 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–CBOE–2020–081. 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–CBOE–2020–081 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[19]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20133 Filed 9–11–20; 8:45 am]

BILLING CODE 8011–01–P

[18] For purposes only of waiving the 30-day operative delay, the Commission also has considered the proposed rule's impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[19] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89782; File No. SR–Phlx–2020–42]

Self-Regulatory Organizations; Nasdaq PHLX LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Rule 3304

September 8, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1], and Rule 19b–4 thereunder,[2] notice is hereby given that on August 27, 2020, Nasdaq PHLX LLC (''Phlx'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. 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 Rule 3304 (Data Feeds Utilized) to add the Long-Term Stock Exchange, Inc. (''LTSE''), MIAX PEARL, LLC (''MIAX PEARL'') and MEMX LLC (''MEMX'') to the list of market centers under Rule 3304 and provide that the Exchange will utilize CQS/UQDF.

The text of the proposed rule change is available on the Exchange's website at *https://listingcenter.nasdaq.com/rulebook/phlx/rules,* 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

In anticipation of their planned launches[3] the Exchange proposes to amend the table in Rule 3304 to include LTSE, MIAX Pearl and MEMX. The Exchange will use securities information processor (''SIP'') data, *i.e.,* CQS SIP data, for securities reported under the Consolidated Quotation System and Consolidated Quotation Plan and UQDF SIP data for securities reported under the Nasdaq Unlisted Trading Privileges Plan to obtain LTSE, MIAX Pearl and MEMX quotation information for the handling, routing and execution of orders, as well as for the regulatory compliance processes related to those functions. At this stage, no secondary source for LTSE, MIAX Pearl or MEMX will be used.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,[4] in general, and furthers the objectives of Section 6(b)(5) of the Act,[5] in particular, in that it is designed to promote just and equitable principles of

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] LTSE plans to begin phase-in production of securities on August, 28, 2020. *See* LTSE Market Announcement available at, *https://assets.ctfassets.net/cchj2z2dcfyd/rnGvgggJUplaIk6N1xNA7/41926d3925a177d6455868090c46aeda/MA-2020-020__Production_Securities_Launching_August_28_-_Google_Docs.pdf.* MIAX Pearl Equities will begin trading in September 2020, pending SEC approval. *See* MIAX Pearl Alerts available at, *https://www.miaxoptions.com/alerts/2020/02/14/miax-pearl-equities-exchange-codes-and-important-dates-regarding-launch-new.* MEMX is expected to launch on September 4, 2020. *See* MEMX Update from Jonathan Kellner, dated June 11, 2020, available at *https://memx.com/memx-update/.*

[4] 15 U.S.C. 78f(b).

[5] 15 U.S.C. 78f(b)(5).

trade, to 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.

The Exchange believes that the proposed rule change removes impediments to and perfects the mechanism of a free and open market because adding LTSE, MIAX Pearl and MEMX because updating its list of market centers for which the Exchange consumes quotation data will provide clarity to market participants. Moreover, it is necessary and consistent with the public interest and the protection of investors to update the Exchange's table of market centers in order to provide transparency with respect to all the direct proprietary and network processor feeds from which the Exchange obtains market data. Additionally, a similar change has been proposed by other exchanges.[6]

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change is not designed to address any competitive issue; instead, its purpose is to enhance transparency with respect to the operation of the Exchange and its use of market data feeds.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act[7] and Rule 19b–4(f)(6) thereunder.[8]

A proposed rule change filed pursuant to Rule 19b–4(f)(6) under the Act[9] normally does not become operative for 30 days after the date of its filing. However, Rule 19b–4(f)(6)(iii)[10] permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has requested that the Commission waive the 30-day operative delay. Waiver of the operative delay would allow the Exchange to disclose the updated list of market centers for which the Exchange consumes quotation data, and the source of the quotation data, at the time that LTSE, MIAX Pearl, and MEMX become operational. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest. Accordingly, the Commission waives the 30-day operative delay and designates the proposed rule change as operative upon filing.[11]

At any time within 60 days of the filing of the 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 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–Phlx–2020–42 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–Phlx–2020–42. 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–Phlx–2020–42 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[12]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20127 Filed 9–11–20; 8:45 am]

BILLING CODE 8011–01–P

[6] *See* Securities Exchange Act Release Nos. 88313 (March 3, 2020), 85 FR 13684 (March 9, 2020) (SR–IEX–2020–03); 88587 (April 8, 2020), 85 FR 20794 (April 14, 2020) (SR–NASDAQ–2020–015); 88601 (April 8, 2020), 85 FR 20798 (April 14, 2020) (NYSE–2020–31); 88604 (April 8, 2020), 85 FR 20741 (April 14, 2020) (SR–NYSECHX–2020–12); 88610 (April 9, 2020), 85 FR 21033 (April 15, 2020) (SR–NYSEARCA–2020–30); 88611 (April 9, 2020), 85 FR 21047 (April 15, 20205) (SR–NYSENAT–2020–15); 89382 (July 23, 2020), 85 FR 45719 (July 29, 2020) (SR–NYSECHX–2020–22); 89369 (July 21, 2020), 85 FR 45270 (July 27, 2020) (SR–NYSE–2020–60); 89387 (July 23, 2020), 85 FR 45722 (July 29, 2020) (SR–NYSEARCA–2020–67); 89388 (July 23, 2020), 85 FR 45711 (July 29, 2020) (SR–NYSENAT–2020–23); 89580 (August 17, 2020), 85 FR 51828 (August 21, 2020) (SR–IEX–2020–11).

[7] 15 U.S.C. 78s(b)(3)(A).

[8] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

[9] 17 CFR 240.19b–4(f)(6).

[10] 17 CFR 240.19b–4(f)(6)(iii).

[11] For purposes only of waiving the 30-day operative delay, the Commission also has considered the proposed rule's impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[12] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89781; File No. SR–NASDAQ–2020–059]

Self-Regulatory Organizations; The Nasdaq Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Equity 7, Section 114(e) and Equity 7, Section 118 of the Fee Schedule

September 8, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on August 31, 2020, The Nasdaq Stock Market LLC (''Nasdaq'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. 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 (i) amend the Exchange's transaction fees to adjust the qualification requirements for certain Qualified Market Maker (''QMM'') fees and rebates at Equity 7, Section 114(e); and (ii) establish new credits and fee tiers and amend the qualification requirements for existing credit tiers at Equity 7, Section 118, as described further below.

The text of the proposed rule change is available on the Exchange's website at *https://listingcenter.nasdaq.com/rulebook/nasdaq/rules,* 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Over the course of the last few months, the Exchange has experimented with various modifications of its pricing schedule with the aim of increasing activity on the Exchange, improving market quality, and increasing market share.[3] Although these changes have met with success, the Exchange continues to examine and amend its pricing schedule to achieve the results it desires. Accordingly, the Exchange proposes to make modifications to its pricing schedule in a further attempt to improve the attractiveness of the market to new and existing market participants.

Changes to Section 114

The Exchange proposes to amend the QMM fees and credits pursuant to Equity 7, Section 114, in two respects.

First, a QMM currently qualifies for the Tier 3 credit if the QMM (i) executes shares of liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs that represent above 1.25% of Consolidated Volume[4] during the month; (ii) quotes at the NBBO at least 25% of the time during the month during regular market hours in an average of at least 2,700 symbols per day; (iii) quotes at the NBBO at least 25% of the time during the month during regular market hours in an average of at least 1,200 symbols in securities in Tape A per day; and (iv) executes shares of liquidity provided in securities in Tape A through one or more of its Nasdaq Market Center MPIDs that represent an increase of at least 0.50% of Consolidated Volume relative to May 2020. The Exchange proposes to offer the rebate per MPID by amending the requirements to provide a credit when a QMM's MPID meets the qualifying criteria. The proposed amendment would remove the current Tier 3 rebate[5] and instead provide an additional $0.00005 per share executed credit for a QMM's MPID if the MPID (i) executes shares of liquidity provided that represents above 1.25% of Consolidated Volume during the month; (ii) quotes at the NBBO at least 50% of the time during the month during regular market hours in an average of at least 2,700 symbols per day; (iii) quotes at the NBBO at least 50% of the time during the month during regular market hours in an average of at least 1,200 symbols in securities in Tape A per day; and (iv) executes shares of liquidity provided that represents an increase of at least 0.50% of Consolidated Volume relative to May 2020. Additionally, the Exchange is proposing clarifying language to explain that, for purposes of this rebate, an MPID is considered to be quoting at the NBBO if the MPID has a displayed order (other than a Designated Retail Order) at either the national best bid or the national best offer or both the national best bid and offer. On a daily basis, the Exchange will determine the number of securities that satisfy the 50% NBBO requirements for the MPID. The QMM would be eligible for the proposed credit in addition to qualifying for the Tier 2 credit. By amending the credit to allow a QMM to qualify at the MPID level, the Exchange intends to provide a further incentive for members to increase their activity on the Exchange that is attributable to adding liquidity and quoting at the NBBO.

Second, the Exchange currently charges a QMM a fee of $0.00295 per share executed for orders in securities listed on exchanges other than Nasdaq priced at $1 or more per share that access liquidity on the Nasdaq Market Center; provided, however, that the QMM's volume of liquidity added through one or more of its Nasdaq Market Center MPIDs during the month (as a percentage of Consolidated Volume) is not less than 0.85%. The Exchange also charges a $0.0029 per share executed fee to QMMs that meet the criteria of Tier 2 or Tier 3 for orders in securities listed on exchanges other than Nasdaq priced at $1 or more per share that access liquidity on the Nasdaq Market Center if the QMM has a combined Consolidated Volume (adding and removing liquidity) of at least 3.7% and MOC/LOC volume greater than 0.25% of Consolidated Volume. The Exchange proposes to modify the requirements for charging a QMM a fee of $0.00295 per share

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* Securities Exchange Act Release Nos. 89343 (July 20, 2020), 85 FR 44941 (July 24, 2020) (SR–Nasdaq–2020–041); 89115 (June 22, 2020), 85 FR 38414 (June 26, 2020) (SR–Nasdaq–2020–030); 87882 (January 2, 2020); 85 FR 939 (January 8, 2020) (SR–Nasdaq–2019–101); 87708 (December 10, 2019), 84 FR 68496 (December 16, 2019) (Nasdaq–2019–094); 85861 (May 15, 2019) 84 FR 23105 (May 21, 2019) (Nasdaq–2019–036).

[4] Pursuant to Equity 7, Section 118(a), the term ''Consolidated Volume'' means the total consolidated volume reported to all consolidated transaction reporting plans by all exchanges and trade reporting facilities during a month in equity securities, excluding executed orders with a size of less than one round lot. For purposes of calculating Consolidated Volume and the extent of a member's trading activity the date of the annual reconstitution of the Russell Investments Indexes is excluded from both total Consolidated Volume and the member's trading activity.

[5] The Exchange is also proposing to remove the asterisk accompanying the current Tier 3 rebate.

executed by increasing the volume of liquidity added from 0.85% to 1.00% during the month (as a percentage of Consolidated Volume). Additionally, the Exchange proposes to modify the requirements for charging a fee of $0.0029 per share executed to a QMM that meets the criteria of Tier 2 by increasing the required MOC/LOC volume from 0.25% to 0.35% of Consolidated Volume, and introducing a new requirement of providing 0.15% or more of Consolidated Volume through midpoint orders. The Exchange also proposes to remove the reference to Tier 3 and make a technical modification by changing the 3.7% qualification requirement for the $0.0029 fee to 3.70%. By modifying the requirements for members to qualify for the lower fee, the Exchange will incentivize members to increase their liquidity, which will promote price discovery and transparency.

Changes to Section 118

The Exchange is also proposing to amend the schedule of fees and credits provided to member organizations, pursuant to Equity 7, Section 118(a), in several respects and amend the Tier A closing cross fees, pursuant to Section 118(d).

First, the Exchange proposes to amend Section 118(a) to charge a fee of $0.0020 to a member entering RTFY orders that remove liquidity from Nasdaq Market Center or that execute in a venue other than the Nasdaq Market Center and has less than a 75% ratio of its RTFY liquidity adding activity to its RTFY total volume. The proposed fee would be applicable to Tape A, Tape B and Tape C and would only apply to orders submitted with the RTFY [6] routing option. By proposing a new fee for participants that have less than a 75% ratio [7] of its RTFY liquidity adding activity to its RTFY total volume, the Exchange hopes to incentivize participants to increase their RTFY liquidity adding activity rather than removing liquidity or submitting orders that route outside of the Exchange. The Exchange also proposes to make a non-substantive change to add the word ''other'' to the RTFY fees that remain at $0.0000 per share executed.

Second, the Exchange proposes to lower the $0.0030 per share executed credit in Section 118(a) to $0.0029 per share executed for a member with shares of liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs that represent 0.625% or more of Consolidated Volume during the month, including shares of liquidity provided with respect to securities that are listed on exchanges other than Nasdaq or NYSE that represent 0.15% or more of Consolidated Volume. The proposed change would be applicable to Tape A, Tape B and Tape C. Although the Exchange is lowering the credit, it is providing members with three additional new credit options as discussed below.

Third, the Exchange proposes to add three new credits in Section 118(a). The Exchange proposes to adopt a credit of $0.00295 per share executed across Tapes A, B and C to a member (i) with shares of liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs that represent 0.70% or more of Consolidated Volume during the month; (ii) executes 0.20% or more of Consolidated Volume during the month through providing midpoint orders and through MELO; and (iii) removes at least 1.10% of Consolidated Volume during the month. The Exchange also proposes to adopt a credit of $0.0030 per share executed across Tapes A, B and C to a member with shares of liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs that represent 1.30% or more of Consolidated Volume during the month, which includes shares of liquidity provided with respect to securities that are listed on exchanges other than Nasdaq or NYSE that represent 0.40% or more of Consolidated Volume. The Exchange also proposes to add a $0.00075 per share executed credit for Tape C securities for certain non-displayed orders that provide liquidity if the member, during the month (i) provides 0.90% or more of Consolidated Volume; (ii) increases providing liquidity through non-displayed orders (other than midpoint orders) by 10% or more relative to the member's July 2020 Consolidated Volume provided through non-displayed orders (other than midpoint orders) and; (iii) provides 0.20% or more Consolidated Volume through non-displayed orders (other than midpoint orders). The Exchange believes that the availability of the three new credits will incentivize members to increase their liquidity adding and removing activity on the Exchange in order to attain one of the new credits. An increase in liquidity adding and removing activity on the Exchange would help to improve the quality of the market for all participants.

Fourth, the Exchange currently provides a credit of $0.0030 per share executed in Section 118(a) to a member with shares of liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs that represent more than 0.75% of Consolidated Volume during the month and provides a daily average of at least 5 million shares of non-displayed liquidity. The Exchange proposes to amend the qualifications by increasing the volume threshold from 0.75% to 1.00%. The Exchange also proposes to remove the requirement for providing a daily average of at least 5 million shares of non-displayed liquidity and to add a requirement that a member's non-displayed liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs represents more than 0.25% of Consolidated Volume.

Lastly, the Exchange currently charges a Tier A fee of $0.0008 per executed share in Section 118(d) for Market-on-Close and Limit-on-Close (''MOC/LOC'') orders for members with shares of liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs that represent above 1.80% of Consolidated Volume or MOC/LOC volume above 0.50% of Consolidated Volume. Additionally, the Exchange currently charges a Tier B fee of $0.0011 per executed share in Section 118(d) for MOC and LOC orders for members with shares of liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs that represent above 0.80% to 1.80% of Consolidated Volume or MOC/LOC volume above 0.30% to 0.50% of Consolidated Volume. The Exchange proposes to lower the volume threshold from 1.80% to 1.75% for Tier A and proposes to make a conforming change for Tier B. Similarly to lowering the volume threshold for credits, by lowering the volume threshold from 1.80% to 1.75%for charging the fee, the Exchange hopes to incentivize members who are close to, but currently do not meet the 1.75% threshold to increase their liquidity in order to qualify for the lower fee.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b)

[6] RTFY is a routing option available for an order that qualifies as a Designated Retail Order under which orders check the System for available shares only if so instructed by the entering firm and are thereafter routed to destinations on the System routing table. If shares remain unexecuted after routing, they are posted to the book. Once on the book, should the order subsequently be locked or crossed by another market center, the System will not route the order to the locking or crossing market center. RTFY is designed to allow orders to participate in the opening, reopening and closing process of the primary listing market for a security. *See* Rule 4748(a)(1)(v)(b).

[7] The ratio is calculated by dividing the participant's RTFY liquidity adding activity on Nasdaq by the participant's total RTFY volume executed on all venues.

of the Act,[8] in general, and furthers the objectives of Sections 6(b)(4) and 6(b)(5) of the Act,[9] in particular, in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility, and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers. The proposal is also consistent with Section 11A of the Act relating to the establishment of the national market system for securities.

The Proposal Is Reasonable

The Exchange's proposed changes to its schedule of fees and credits are reasonable in several respects. As a threshold matter, the Exchange is subject to significant competitive forces in the market for equity securities transaction services that constrain its pricing determinations in that market. The fact that this market is competitive has long been recognized by the courts. In *NetCoalition* v. *Securities and Exchange Commission,* the D.C. Circuit stated as follows: ''[n]o one disputes that competition for order flow is 'fierce.' . . . As the SEC explained, '[i]n the U.S. national market system, buyers and sellers of securities, and the broker-dealers that act as their order-routing agents, have a wide range of choices of where to route orders for execution'; [and] 'no exchange can afford to take its market share percentages for granted' because 'no exchange possesses a monopoly, regulatory or otherwise, in the execution of order flow from broker dealers'. . . .'' [10]

The Commission and the courts have repeatedly expressed their preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, while adopting a series of steps to improve the current market model, 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.'' [11]

Numerous indicia demonstrate the competitive nature of this market. For example, clear substitutes to the Exchange exist in the market for equity security transaction services. The Exchange is only one of several equity venues to which market participants may direct their order flow. Competing equity exchanges offer similar tiered pricing structures to that of the Exchange, including schedules of rebates and fees that apply based upon members achieving certain volume thresholds. [12]

Within this environment, market participants can freely and often do shift their order flow among the Exchange and competing venues in response to changes in their respective pricing schedules. As such, the proposal represents a reasonable attempt by the Exchange to increase its liquidity and market share relative to its competitors.

The Exchange has designed its proposed schedule of credits and charges to provide increased overall incentives to members to increase their liquidity removal and adding activity on the Exchange. An increase in liquidity removal and adding activity on the Exchange will, in turn, improve the quality of the Nasdaq market and increase its attractiveness to existing and prospective participants. Generally, the proposed new credits and charges will be comparable to, if not favorable to, those that its competitors provide.[13]

Moreover, the Exchange believes that it is reasonable to modify certain fees and credits within its fee schedule as a means of incentivizing market participants to increase their contributions to the improvement of the quality of the Exchange.

In particular, the Exchange believes that it is reasonable to create a stricter qualification for the additional rebate of $0.00005 per share executed for a QMM and to apply the qualifications to each MPID because the activity of QMMs that currently qualify for the Tier 3 credit has grown, such that an increase in credit qualifying criteria is needed to ensure that this credit remains relevant to current levels of liquidity providing activity on the Exchange and continues to incentivize QMMs to provide liquidity and quote at the NBBO in more securities. To the extent that this proposal results in an increase in liquidity adding and quoting activity on the Exchange, this will improve the quality of the Nasdaq market and increase its attractiveness to existing and prospective participants.

Additionally, the Exchange believes it is reasonable to increase the volume threshold for the QMM fees. By increasing the volume threshold and adding a new threshold requirement for liquidity adding activity to qualify for the lower fee, the Exchange hopes to incentivize liquidity adding activity on the Exchange.

The Exchange also believes that it is reasonable to charge a fee of $0.0020 per share executed in Section 118(a) to a member entering RTFY orders that remove liquidity from Nasdaq Market Center or that execute on a venue other than the Nasdaq Market Center and has less than a 75% ratio of its RTFY liquidity adding activity to its RTFY total volume. Since the inception of the RTFY routing option, there has been no charge to participants entering RTFY orders even if the order ultimately executes on the Exchange.[14] Retail order flow firms benefit from the RTFY routing option by not incurring liquidity removal fees while obtaining potential price improvements and better execution quality. By proposing a new fee for participants that have less than a 75% ratio of its RTFY liquidity adding activity to its RTFY total volume, the Exchange hopes to incentivize participants to increase their RTFY liquidity adding activity rather than removing liquidity or submitting orders that route outside of the Exchange.

The Exchange believes that it is reasonable to lower the $0.0030 per share executed credit in Section 118(a) to $0.0029 per share executed because the Exchange is proposing three new credit options for members to qualify for.

Moreover, the Exchange believes it is reasonable to add three new credits to Section 118(a). The Exchange believes that the availability of the three new credits will incentivize members to increase their liquidity adding and removing activity on the Exchange in order to attain one of the new credits. An increase in liquidity adding and removing activity on the Exchange would help to improve the quality of the market for all participants.

Additionally, the Exchange believes that it is reasonable to modify the Section 118(a) requirements for the credit of $0.0030 per share executed by increasing the volume threshold from 0.75% to 1.00% and removing the requirement for providing a daily average of at least 5 million shares of non-displayed liquidity and adding a requirement that a member's non-

[8] 15 U.S.C. 78f(b).

[9] 15 U.S.C. 78f(b)(4) and (5).

[10] *NetCoalition* v. *SEC,* 615 F.3d 525, 539 (D.C. Cir. 2010) (quoting Securities Exchange Act Release No. 59039 (December 2, 2008), 73 FR 74770, 74782–83 (December 9, 2008) (SR–NYSEArca–2006–21)).

[11] Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496, 37499 (June 29, 2005) (''Regulation NMS Adopting Release'').

[12] As an example, CBOE EDGX provides a standard rebate for liquidity adders of $0.00170 per share executed (or between $0.0020 and $0.0029) per share executed if a member qualifies for a volume tier.

[13] *Id.*

[14] *See* Securities Exchange Act Release No. 75987 (September 25, 2015), 80 FR 59210 (October 1, 2015) (SR–Nasdaq–2015–112).

displayed liquidity provided in all securities through one or more of its Nasdaq Market Center MPIDs represents more than 0.25% of Consolidated Volume. By increasing the volume threshold for displayed liquidity and changing the requirement for the shares of non-displayed liquidity, the Exchange believes it will incentivize members to increase the extent of their liquidity adding activity on the Exchange to qualify for and to continue to qualify for this credit.

Similarly to lowering the volume threshold for credits, the Exchange believes that it is reasonable to lower the volume threshold in Section 118(d) for MOC and LOC fees from 1.80% to 1.75% for Tiers A and B because the Exchange hopes to incentivize members who are close to, but currently do not meet the 1.75% threshold to increase their liquidity in order to qualify for the lower fee.

To the extent that these proposed changes lead to an increase in overall liquidity activity on the Exchange and more competitive pricing, this will improve the quality of the Exchange's market and increase its attractiveness to existing and prospective participants. The Exchange notes that those market participants that are dissatisfied with the new fees or credits are free to shift their order flow to competing venues that offer them lower charges or higher credits.

The Proposal Is an Equitable Allocation of Credits

The Exchange believes its proposal will allocate its credits and fees fairly among its market participants. The proposal will amend the $0.00005 per share executed credit for QMMs in Section 114 to allow a QMM to qualify at the MPID level. It is equitable to make the qualification requirement in Section 114 stricter for the additional rebate of $0.00005 per share executed for QMMs as a means of ensuring the credit remains relevant to current levels of liquidity providing activity on the Exchange. By amending the credit to allow a QMM to qualify at the MPID level, the Exchange intends to provide a further incentive for members to increase their activity on the Exchange that is attributable to adding liquidity and quoting at the NBBO. An increase in liquidity providing activity on the Exchange will improve the quality of the Nasdaq market and increase its attractiveness to existing and prospective participants.

Furthermore, the Exchange also believes that it is equitable to establish three new credits in Section 118(a). In particular, the Exchange believes that it is equitable to establish a new $0.00295 per share executed credit in Tapes A, B and C and a new $0.0030 per share executed credit in Tapes A, B and C as a means of incentivizing members to provide and remove meaningful amounts of liquidity to the Exchange. To the extent that the Exchange succeeds in increasing liquidity adding and removal activity on the Exchange and in attracting additional order flow, then the Exchange would experience improvements in its market quality, which would benefit all market participants. Further, the Exchange believes it is equitable to lower the $0.0030 per share executed credit to $0.0029 because the Exchange has added two new credits with the Exchange's goal to promote increased liquidity. An increase in overall liquidity adding activity on the Exchange will improve the quality of the Nasdaq market and increase its attractiveness to existing and prospective participants.

Lastly, the Exchange believes it is equitable to provide a $0.00075 per share executed credit for other non-displayed orders in Tape C securities. The Exchange believes it is equitable for the Exchange to propose a credit for members with non-displayed orders in securities in Tapes C due to the Exchange's goal to specifically promote increased liquidity in securities in Tape C. Additionally, the Exchange has not seen the level of volume in Tape C that it has expected. An increase in overall liquidity adding activity on the Exchange will improve the quality of the Nasdaq market and increase its attractiveness to existing and prospective participants.

The Proposal Is an Equitable Allocation of Fees

The Exchange believes its proposal will allocate its fees fairly among its market participants. It is equitable to modify the fees to members who execute MOC and LOC orders in the closing cross in Section 118(d) and the fees to members whose RTFY orders remove liquidity or are routed out of the Exchange.

In particular, the Exchange believes it is equitable for the Exchange to charge a fee of $0.0020 to a member entering RTFY orders that remove liquidity from Nasdaq Market Center or that execute in a venue other than the Nasdaq Market Center and has less than a 75% ratio of its RTFY liquidity adding activity to its RTFY total volume. By adding this fee, the Exchange hopes to incentivize participants to increase their RTFY liquidity adding activity rather than removing liquidity or submitting orders that route outside of the Exchange. Additionally, the Exchange believes that the fee will encourage market participants to increase their liquidity adding activity.

Additionally, it is equitable for the Exchange to lower the volume threshold for obtaining the $0.0008 per executed share fee for MOC and LOC orders by incentivizing members to increase their liquidity in order to qualify for the lowest closing cross fee offered by the exchange.

Furthermore, it is equitable for the Exchange to increase the volume threshold and add a new threshold requirement for QMM liquidity adding activity to qualify for the lower fees because increasing the volume threshold, the Exchange hopes to incentivize liquidity adding activity on the Exchange.

The Proposed Amended Credits Are Not Unfairly Discriminatory

The Exchange believes that the proposal is not unfairly discriminatory. As an initial matter, the Exchange believes that nothing about its volume-based tiered pricing model is inherently unfair; instead, it is a rational pricing model that is well-established and ubiquitous in today's economy among firms in various industries—from co-branded credit cards to grocery stores to cellular telephone data plans—that use it to reward the loyalty of their best customers that provide high levels of business activity and incent other customers to increase the extent of their business activity. It is also a pricing model that the Exchange and its competitors have long employed with the assent of the Commission. It is fair because it incentivizes customer activity that increases liquidity, enhances price discovery, and improves the overall quality of the equity markets.

Although Section 114(e) of the Exchange's proposal to allow a QMM to qualify for an additional $0.00005 per share executed credit will require that a QMM meet the criteria at the MPID level, any resulting increase in liquidity on the Exchange will improve market-wide quality and price discovery, to the benefit of all participants. Moreover, to the extent that the proposal causes members to increase the extent of their liquidity adding and quoting activity on the Exchange, the Exchange market quality will improve, and all market participants will benefit. Moreover, any market participant that does not wish to receive lower a credit is free to shift its order flow to a competing venue.

The Exchange also believes that its three proposed new credits in Section 118(a) are not unfairly discriminatory.

These proposed credits stand to improve the overall market quality of the Exchange, to the benefit of all market participants, by incentivizing members to provide meaningful amounts of liquidity to the Exchange, including in securities in Tape C. Additionally, it is not unfairly discriminatory to target the $0.00075 per share executed credit in Tape C, in part, to increase activity in other non-displayed orders, because attracting additional order flow stands to benefit all market participants. Likewise, it is not unfairly discriminatory to target the $0.00075 per share executed credit, in part, to liquidity adding activity in securities in Tape C, because the Exchange believes that the market for such securities would benefit from additional liquidity. As discussed above the Exchange has not seen the level of volume in Tape C that it has expected. The Exchange notes that it has limited funds to apply in the form of incentives, and thus must deploy those limited funds to incentives that it believes will be the most effective at improving market quality in areas that the Exchange determines are in need of improvement.

The Proposed Amended Fees Are Not Unfairly Discriminatory

The Exchange believes that the proposal is not unfairly discriminatory. Nasdaq currently charges a QMM a fee of $0.0030 per share executed for orders in Nasdaq-listed securities priced at $1 or more per share that access liquidity on the Nasdaq Market Center. The Exchange currently charges a QMM a fee of $0.00295 per share and $0.0029 per share if the QMM meets certain volume thresholds. It is not unfairly discriminatory for the Exchange to increase the volume thresholds for these fees and and to add a new volume thresholds for the $0.0029 per share fee because an increase in overall liquidity adding activity on the Exchange will improve the quality of the Nasdaq market and increase its attractiveness to existing and prospective market participants.

The Exchange does not believe that it is discriminatory to charge a fee of $0.0020 to a member entering RTFY orders that remove liquidity Nasdaq Market Center or that execute in a venue other than the Nasdaq Market Center and has less than a 75% ratio of its RTFY liquidity adding activity to its RTFY total volume. The Exchange is proposing to add the fee to Tapes A, B and C. By adding this fee related to RTFY volume, the Exchange hopes to incentivize participants to increase their RTFY liquidity adding activity rather than removing liquidity or submitting orders that route outside of the Exchange. Similarly, the Exchange does not believe it is discriminatory to lower the volume threshold for obtaining the $0.0008 per executed share fee for MOC and LOC orders because it will incentivize members to increase their liquidity adding activity in order to obtain the lower fee, which enhances price discovery, and improves the overall quality of the equity markets.

Moreover, any market participant that does not wish to pay higher charges is free to shift its order flow to a competing venue.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

Intramarket Competition

The Exchange does not believe that its proposals will place any category of Exchange participant at a competitive disadvantage. To the contrary, the proposed changes will provide opportunities for members to receive new and amended credits or lower fees based on their market-improving behavior. Any member may elect to provide the levels of market activity required in order to receive the new or amended credits or lower fees. Furthermore, all members of the Exchange will benefit from any increase in market activity that the proposals effectuates.

Moreover, members are free to trade on other venues to the extent they believe that the credits provided are too low or the qualification criteria are not attractive. As one can observe by looking at any market share chart, price competition between exchanges is fierce, with liquidity and market share moving freely between exchanges in reaction to fee and credit changes. The Exchange notes that the tier structure is consistent with broker-dealer fee practices as well as the other industries, as described above.

Intermarket Competition

The Exchange believes that its proposed modification to its schedule of credits will not impose a burden on competition because the Exchange's execution services are completely voluntary and subject to extensive competition both from the other 12 live exchanges and from off-exchange venues, which include 34 alternative trading systems. The Exchange notes that it operates in a highly competitive market in which market participants can readily favor competing venues if they deem fee levels at a particular venue to be excessive, or rebate opportunities available at other venues to be more favorable. In such an environment, the Exchange must continually adjust its fees and credits to remain competitive with other exchanges and with alternative trading systems that have been exempted from compliance with the statutory standards applicable to exchanges. Because competitors are free to modify their own fees in response, and because market participants may readily adjust their order routing practices, the Exchange believes that the degree to which fee and credit changes in this market may impose any burden on competition is extremely limited.

The proposed amended fees and credits are reflective of this competition because, even as one of the largest U.S. equities exchanges by volume, the Exchange has less than 18% market share, which in most markets could hardly be categorized as having enough market power to burden competition. Moreover, as noted above, price competition between exchanges is fierce, with liquidity and market share moving freely between exchanges in reaction to fee and credit changes. This is in addition to free flow of order flow to and among off-exchange venues which comprised more than 43% of industry volume for the month of July 2020.

The Exchange's proposals are pro-competitive in that the Exchange intends for them to increase liquidity on the Exchange and thereby render the Exchange a more attractive and vibrant venue to market participants.

In sum, if the changes proposed herein are unattractive to market participants, it is likely that the Exchange will lose market share as a result. Accordingly, the Exchange does not believe that the proposed changes will impair the ability of members or competing order execution venues to maintain their competitive standing in the financial markets.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Pursuant to Section 19(b)(3)(A)(ii) of the Act,[15] the Exchange has designated this proposal as establishing or changing a due, fee, or other charge imposed by the self-regulatory organization on any person, whether or not the person is a member of the self-regulatory organization, which renders the proposed rule change effective upon filing.

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is: (i) Necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule 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–NASDAQ–2020–059 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–NASDAQ–2020–059. 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–NASDAQ–2020–059 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[16]

J. Matthew DeLesDernier,

Assistant Secretary.

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[15] 15 U.S.C. 78s(b)(3)(A)(ii).

[16] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89786; File No. SR–MIAX–2020–30]

Self-Regulatory Organizations; Miami International Securities Exchange, LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Adopt Exchange Rule 1326, Transfer of Positions

September 8, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the ''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on September 4, 2020, Miami International Securities Exchange, LLC (''MIAX'' or the ''Exchange'') filed with the Securities and Exchange Commission (the ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Exchange filed the proposal as a ''non-controversial'' proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act [3] and Rule 19b–4(f)(6) thereunder.[4] 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 is filing a proposal to adopt new Exchange Rule 1326, Transfer of Positions.

The text of the proposed rule change is available on the Exchange's website at *http://www.miaxoptions.com/rule-filings/* at MIAX's principal office, 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. *Purpose*

The Exchange proposes to adopt new Exchange Rule 1326, Transfer of Positions, to provide a process by which Members [5] may transfer option positions in limited circumstances. This proposed rule specifies the specific limited circumstances under which a Member may effect transfers of positions. This rule would permit market participants to move positions from one account to another without first exposure of the transaction on the Exchange. This rule would permit transfers upon the occurrence of significant, non-recurring events. The proposed rule change is similar to Nasdaq ISE Options 6, Section 5.

Currently, the rules of the Exchange do not specifically address transfers of option positions between accounts, individuals, or entities. The Exchange, however, plans on aligning its Rule with its competitors by allowing transfers in situations similar to those permitted on other exchanges. The proposed rule will

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] 15 U.S.C. 78s(b)(3)(A)(iii).

[4] 17 CFR 240.19b–4(f)(6).

[5] The term ''Member'' means an individual or organization approved to exercise the trading rights associated with a Trading Permit. Members are deemed ''members'' under the Exchange Act. *See* Exchange Rule 100.

establish Exchange policy with respect to transfers of options positions in certain limited circumstances.

Permissible Transfers

The Exchange proposes to adopt new Exchange Rule 1326, titled ''Transfer of Positions'' to provide for the circumstances pursuant to which Members may transfer their options positions without first exposing the order. This rule states that a Member must be on at least one side of the transfer. This rule is similar to Nasdaq ISE Options 6, Section 5.

The Exchange proposes to provide in paragraph (a) that, existing positions in options listed on the Exchange of a Member, or non-Member, that are to be transferred on, from, or to the books of a Clearing Member [6] may be transferred off the Exchange if the transfer involves one or more of the following events:

(1) Pursuant to Rule 301, an adjustment or transfer in connection with the correction of a bona fide error in the recording of a transaction or the transferring of a position to another account, provided that the original trade documentation confirms the error;

(2) the transfer of positions from one account to another account where no change in ownership is involved (*i.e.,* accounts of the same Person (as defined in Rule 100)), provided the accounts are not in separate aggregation units or otherwise subject to information barrier or account segregation requirements;

(3) the consolidation of accounts where no change in ownership is involved;

(4) a merger, acquisition, consolidation, or similar non-recurring transaction for a Person;

(5) the dissolution of a joint account in which the remaining Member assumes the positions of the joint account;

(6) the dissolution of a corporation or partnership in which a former nominee of the corporation or partnership assumes the positions;

(7) positions transferred as part of a Member's capital contribution to a new joint account, partnership, or corporation;

(8) the donation of positions to a not-for-profit corporation;

(9) the transfer of positions to a minor under the Uniform Gifts to Minors Act; or

(10) the transfer of positions through operation of law from death, bankruptcy, or otherwise.

The proposed rule change makes clear that the transferred positions must be on, from, or to the books of a Clearing Member. The proposed rule change states that existing positions of a Member or a non-Member may be subject to a transfer, except under specified circumstances in which a transfer may only be effected for positions of a Member.[7] The Exchange notes transfers of positions in Exchange listed options may also be subject to applicable laws, rules, and regulations, including rules of other self-regulatory organizations.[8] Except as explicitly provided in the proposed rule text, the proposed rule change is not intended to exempt position transfers from any other applicable rules or regulations, and proposed paragraph (h) makes this clear in the rule.

The proposed Exchange Rule 1326(b) codifies Exchange guidance regarding certain restrictions on permissible transfers relating to netting of open positions and to margin and haircut treatment, unless otherwise permitted by paragraph (f). No position may net against another position (''netting''), and no position transfer may result in preferential margin or haircut treatment.[9] Netting occurs when long positions and short positions in the same series ''offset'' against each other, leaving no position, or a reduced position. For example, if a Member wanted to transfer 100 long calls to another account that contained short calls of the same options series as well as other positions, even if the transfer is permitted pursuant to one of the ten permissible events listed in the Proposed Rule, the Member could not transfer the offsetting series, as they would net against each other and close the positions.

However, netting is permitted for transfers on behalf of a Market Maker account for transactions in multiply listed options series on different options exchanges, but only if the Market Maker nominees are trading for the same Member, and the options transactions on the different options exchanges clear into separate exchange-specific accounts because they cannot easily clear into the same Market Maker account at the Clearing Corporation. In such instances, all Market Maker positions in the exchange-specific accounts for the multiply listed class would be automatically transferred on their trade date into one central Market Maker account (commonly referred to as a ''universal account'') at the Clearing Corporation. Positions cleared into a universal account would automatically net against each other. Option exchanges permit different naming conventions with respect to Market Maker account acronyms (for example, lettering versus numbering and number of characters), which are used for accounts at the Clearing Corporation. A Market Maker may have a nominee with an appointment in class XYZ on the Exchange, and have another nominee with an appointment in class XYZ on another exchange, but due to account acronym naming conventions, those nominees may need to clear their transactions into separate accounts (one for Exchange transactions and another for transactions on the other exchange) at the Clearing Corporation rather than into a universal account (in which account the positions may net). The proposed rule change permits transfers from these separate exchange-specific accounts into the Market Maker's universal account in this circumstance to achieve this purpose.

Transfer Price

The Exchange proposes to state that the transfer price, to the extent it is consistent with applicable laws, rules, and regulations, including rules of other self-regulatory organizations, and tax and accounting rules and regulations, at which a transfer is effected may be: (1) The original trade prices of the positions that appear on the books of the trading Clearing Member, in which case the records of the transfer must indicate the original trade dates for the positions; provided, transfers to correct bona fide errors pursuant to proposed subparagraph (a)(1) must be transferred at the correct original trade prices; (2) mark-to-market prices of the positions at the close of trading on the transfer date; (3) mark-to-market prices of the positions at the close of trading on the trade date prior to the transfer date;[10] or (4) the then-current market price of the positions at the time the transfer is effected.[11]

This proposed rule change provides market participants that effect transactions with flexibility to select a transfer price based on the circumstances of the transfer and their business. However, for corrections of bona fide errors, because those transfers

[6] The term ''Clearing Member'' means a Member that has been admitted membership in the Clearing Corporation pursuant to the provisions of the rules of the Clearing Corporation. *See* Exchange Rule 100.

[7] *See* proposed paragraph (a)(5) and (7).

[8] *See* proposed paragraph (h).

[9] For example, positions may not transfer from a customer, joint back office, or firm account to a Market Maker account. However, positions may transfer from a Market Maker account to a customer, joint back office, or firm account (assuming no netting of positions occurs).

[10] For example, for a transfer that occurs on a Tuesday, the transfer price may be based on the closing market price on Monday.

[11] *See* proposed paragraph (c).

are necessary to correct processing errors that occurred at the time of the transaction, those transfers would occur at the original transaction price, as the purpose of the transfer is to create the originally intended result of the transaction.

Prior Written Notice

Proposed Exchange Rule 1326(d) requires a Member and its Clearing Member(s) (to the extent the Member is not self-clearing) to submit to the Exchange, in a manner determined by the Exchange, written notice prior to effecting a transfer from or to the account(s) of a Member.[12] The notice must indicate: The Exchange-listed options positions to be transferred; the nature of the transaction; the enumerated provision(s) under proposed paragraph (a) pursuant to which the positions are being transferred; the name of the counterparty(ies); the anticipated transfer date; the method for determining the transfer price; and any other information requested by the Exchange.[13] The proposed notice will ensure the Exchange is aware of all transfers so that it can monitor and review them (including the records that must be retained pursuant to proposed paragraph (e)) to determine whether they are effected in accordance with the Rules.

Additionally, requiring notice from the Member(s) and its Clearing Member(s) will ensure both parties are in agreement with respect to the terms of the transfer. As noted in proposed subparagraph (d)(2), receipt of notice of a transfer does not constitute a determination by the Exchange that the transfer was effected or reported in conformity with the requirements of proposed Rule 1326. Notwithstanding submission of written notice to the Exchange, Members and Clearing Members that effect transfers that do not conform to the requirements of the proposed Rule will be subject to appropriate disciplinary action in accordance with the Rules.

Records

The proposed Exchange Rule 1326(e) requires that each Member and each Clearing Member that is a party to a transfer must make and retain records of the information provided in the written notice to the Exchange pursuant to proposed subparagraph (e), as well as information on the actual Exchange-listed options that are ultimately transferred, the actual transfer date, and the actual transfer price (and the original trade dates, if applicable), and any other information the Exchange may request the Member or Clearing Member to provide.[14]

Presidential Exemption

Proposed paragraph 1326(f) provides exemptions approved by the Exchange's Chief Executive Officer or President (or senior-level designee). Specifically, this provision is in addition to the exemptions set forth in proposed paragraph (a). The Exchange proposes that the Exchange Chief Executive Officer or President (or senior-level designee) may grant an exemption from the requirement of this proposed Rule, on his or her own motion or upon application of the Member (with respect to the Member's positions) or a Clearing Member (with respect to positions carried and cleared by the Clearing Members). The Chief Executive Officer, the President, or his or her designee, may permit a transfer if necessary or appropriate for the maintenance of a fair and orderly market and the protection of investors and is in the public interest, including due to unusual or extraordinary circumstances. For example, an exemption may be granted if the market value of the Person's positions would be compromised by having to comply with the requirement to trade on the Exchange pursuant to the normal auction process or when, in the judgment of the Chief Executive Officer, President, or his or her designee, market conditions make trading on the Exchange impractical.[15]

Routine, Recurring Transfers

The Exchange proposes to state that the transfer procedure set forth in Rule 1326 is intended to facilitate non-routine, nonrecurring movements of positions.[16] The transfer procedure is not to be used repeatedly or routinely in circumvention of the normal auction market process.

Exchange-Listed Options

Lastly, the Exchange proposes paragraph (h) which notes that the transfer procedure set forth in the proposed Rule is only applicable to positions in options listed on the Exchange. Transfers of positions in Exchange-listed options may also be subject to applicable laws, rules, and regulations, including rules of other self-regulatory organizations. Transfers of non-Exchange listed options and other financial instruments are not governed by this proposed Rule.

2. Statutory Basis

The Exchange believes that its proposed rule change is consistent with Section 6(b) of the Act[17] in general, and furthers the objectives of Section 6(b)(5) of the Act[18] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanisms of a free and open market and a national market system and, in general, to protect investors and the public interest.

Specifically, the Exchange believes the proposed transfer rule is consistent with the Section 6(b)(5)[19] requirements that the rules of an exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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. Additionally, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)[20] requirement that the rules of an exchange not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Exchange believes that permitting transfers in very limited circumstances is reasonable to allow a Member to accomplish certain goals efficiently. The proposed rule permits transfers in situations involving dissolutions of entities or accounts, for purposes of donations, mergers or by operation of law. As noted above for example, a Member that is undergoing a structural change and a one-time movement of positions may require a transfer of positions or a Member that is leaving a firm that will no longer be in business

[12] This notice provision applies only to transfers involving a Member's positions and not to positions of non-Members parties, as they are not subject to the Rules. In addition, no notice would be required to effect transfers to correct bona fide errors pursuant to proposed subparagraph (a)(1) or transfers of positions from one account to another where no change in ownership is involved pursuant to proposed paragraph (a)(2).

[13] *See* proposed paragraph (d)(1).

[14] *See* proposed paragraph (e).

[15] *See* proposed paragraph (f).

[16] *See* proposed paragraph (g).

[17] 15 U.S.C. 78f(b).

[18] 15 U.S.C. 78f(b)(5).

[19] 15 U.S.C. 78f(b)(5).

[20] *Id.*

may require a transfer of positions to another firm. Also, a Member may require a transfer of positions to make a capital contribution. The above-referenced circumstances are non-recurring situations where the transferor continues to maintain some ownership interest or manage the positions transferred. By contrast, repeated or routine transfers between entities or accounts—even if there is no change in beneficial ownership as a result of the transfer—is inconsistent with the purposes for which the proposed rule will be adopted. Accordingly, the Exchange believes that such activity should not be permitted under the rules and thus, seeks to adopt language in proposed paragraph (g) that the transfer of positions procedures set forth in the proposed rule are intended to facilitate non-recurring movements of positions.

The proposed rule change will provide market participants that experience these limited, non-recurring events with an efficient and effective means to transfer positions in these situations. The Exchange believes the proposed rule change regarding permissible transfer prices provides market participants with flexibility to determine the price appropriate for their business, which maintain cost bases in accordance with normal accounting practices and removes impediments to a free and open market.

The proposed rule change which requires notice and maintenance of records will ensure the Exchange is able to review transfers for compliance with the Rules, which prevents fraudulent and manipulative acts and practices. The requirement to retain records is consistent with the requirements of Rule 17a–3 and 17a–4 under the Act.

Similar to Nasdaq ISE and Cboe rules,[21] the Exchange would permit a presidential exemption. The Exchange believes that this exemption is consistent with the Act because the Exchange's Chief Executive Officer or President (or senior-level designee) would consider an exemption in very limited circumstances. The transfer process is intended to facilitate non-routine, nonrecurring movements of positions and, therefore, is not to be used repeatedly or routinely in circumvention of the normal auction market process. The proposed Rule specifically provides within the rule text that the Exchange's Chief Executive Officer or President (or senior-level designee) may in his or her judgment allow a transfer if it is necessary or appropriate for the maintenance of a fair and orderly market and the protection of investors and is in the public interest, including due to unusual or extraordinary circumstances such as the market value of the Person's positions will be comprised by having to comply with the requirement to trade on the Exchange pursuant to the normal auction process or, when in the judgment of the President or his or her designee, market conditions make trading on the Exchange impractical. These standards within paragraph (f) of the proposed rule are intended to provide guidance concerning the use of this exemption which is intended to provide the Exchange with the ability to utilize the exemption for the maintenance of a fair and orderly market and the protection of investors and is in the public interest. The Exchange believes that the exemption is consistent with the Act because it would allow the Exchange's Chief Executive Officer or President (or senior-level designee) to act in certain situations which comply with the guidance within paragraph (f) which is intended to protect investors and the general public. Although Cboe's rule grants an exemption to the President (or senior-level designee),[22] the Exchange has elected to parallel the Nasdaq ISE and grant an exemption to the Exchange's Chief Executive Officer or President (or senior-level designee), who are similarly situated within the Exchange's organization as senior-level individuals.[23]

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

The Exchange does not believe the proposed rule change will impose an undue burden on intra-market competition as the transfer procedure may be utilized by any Member and the rule will apply uniformly to all Members. Use of the transfer procedure is voluntary, and all Members may use the procedure to transfer positions as long as the criteria in the proposed rule are satisfied. With the establishment of the proposed rule, a Member that experiences limited permissible, non-recurring events would have an efficient and effective means to transfer positions in these situations. The Exchange believes the proposed rule change regarding permissible transfer prices provides market participants with flexibility to determine the price appropriate for their business, which determine prices in accordance with normal accounting practices and removes impediments to a free and open market. The Exchange does not believe the proposed notice and record requirements are unduly burdensome to market participants. The Exchange believes the proposed requirements are reasonable and will ensure the Exchange is aware of transfers and would be able to monitor and review the transfers to ensure the transfer falls within the proposed rule.

Adopting an exemption, similar to Nasdaq ISE Options 6, Section 5(f), to permit the Exchange's Chief Executive Officer or President (or senior-level designees) to grant an exemption, in addition to the limited circumstances of the proposed rule, in his or her judgment, does not impose an undue burden on competition. Such an exemption would only be applied when in the judgement of the Chief Executive Officer, or President or his or her designee, the transfer is necessary or appropriate for the maintenance of a fair and orderly market and the protection of investors and is in the public interest, including due to unusual or extraordinary circumstances, such as the possibility that the market value of a Person's positions would be compromised by having to comply with the requirement to trade on the Exchange pursuant to the normal auction process or when market conditions make trading on the Exchange impractical.

The Exchange does not believe the proposed rule change will impose an undue burden on inter-market competition. The proposed position transfer procedure is not intended to be a competitive trading tool. The proposed rule change permits, in limited circumstances, a transfer to facilitate non-routine, nonrecurring movements of positions. As provided for in proposed paragraph (g), it would not be used repeatedly or routinely in circumvention of the normal auction market process. In addition, proposed paragraph (f) provides within the rule text that the Exchange's Chief Executive Officer or President (or senior-level designee) may in his or her judgment allow a transfer for the maintenance of a fair and orderly market and the protection of investors and is in the public interest. The Exchange believes that the exemption does not impose an undue burden on competition as the Exchange's Chief Executive Officer or President (or senior-level designee) would apply the exemption consistent with the guidance laid out in the

[21] *See* Nasdaq ISE Options 6, Section 5; and Cboe Rule 6.7.

[22] *See* Cboe Rule 6.7(f).

[23] *See* Nasdaq ISE Options 6, Section 5(f).

proposed rule text. Additionally, as discussed above, the proposed rule change is similar to Cboe Rule 6.7 and Nasdaq ISE Options 6, Section 5. The Exchange believes having similar rules related to position transfers to those of other options exchanges will reduce the administrative burden on market participants of determining whether their transfers comply with multiple sets of rules.

As such, the Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act [24] and Rule 19b–4(f)(6) thereunder.[25]

A proposed rule change filed under Rule 19b–4(f)(6) [26] normally does not become operative for 30 days after the date of the filing. However, pursuant to Rule 19b–4(f)(6)(iii),[27] the Commission may designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay to so that it may adopt the proposed position transfer rules as soon as possible which, according to the Exchange, would benefit investors and the general public because it will provide Members with the ability to request a transfer, for limited, non-recurring types of transfers, without the requirement for exposing those orders on the Exchange. The Commission believes that waiver of the operative delay is consistent with the protection of investors and the public interest because the proposed rule change does not present any unique or novel regulatory issues and is substantively identical to provisions in Cboe Rule 6.7 and Nasdaq ISE Options 6, Section 5. Accordingly, the Commission hereby waives the operative delay and designates the proposal operative upon filing.[28]

At any time within 60 days of the filing of the 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 will institute proceedings 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–MIAX–2020–30 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–MIAX–2020–30. 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–MIAX–2020–30 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[29]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20130 Filed 9–11–20; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89784; File No. SR–MEMX–2020–06]

Self-Regulatory Organizations; MEMX LLC; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Adopt Rule 15.3, Collection of Exchange Fees and Other Claims and Billing Policy

September 8, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on August 28, 2020, MEMX LLC ("MEMX" or the "Exchange") filed with the Securities and Exchange Commission (the "Commission") the proposed rule change as described in Items I, and II below, which Items have been prepared by the Exchange. The Exchange filed the proposal as a "non-controversial" proposed rule change pursuant to Section 19(b)(3)(A)(iii) of the Act [3] and Rule 19b–4(f)(6) thereunder.[4] The Commission is publishing this notice to

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[24] 15 U.S.C. 78s(b)(3)(A).

[25] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

[26] 17 CFR 240.19b–4(f)(6).

[27] 17 CFR 240.19b–4(f)(6)(iii).

[28] For purposes only of waiving the 30-day operative delay, the Commission has also considered the proposed rule's impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[29] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] 15 U.S.C. 78s(b)(3)(A).

[4] 17 CFR 240.19b–4.

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 is filing with the Commission a proposed rule change to proposed rule change to adopt Rule 15.3 and entitle it ''Collection of Exchange Fees and Other Claims and Billing Policy'' that (a) requires each member of the Exchange (''Member''), and all applicants for membership, to provide one or more clearing account numbers that correspond to an account(s) at the National Securities Clearing Corporation (''NSCC'') for purposes of permitting the Exchange to debit certain fees, fines, charges and/or other monetary sanctions or other monies due and owing to the Exchange; and (b) require Members to submit billing disputes within a certain time period. The text of the proposed rule change is provided in Exhibit 5.

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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to adopt Rule 15.3 to (a) require each Member, and all applicants for membership, to provide one or more clearing account numbers that correspond to an account(s) at the NSCC for purposes of permitting the Exchange to debit certain fees, fines, charges, and/or other monetary sanctions or other monies due and owing to the Exchange; and (b) require Members to submit billing disputes within a certain time period.

Direct Debit Process

Paragraph (a) of the proposed Rule 15.3 requires Members, and all applicants for membership, to provide one or more clearing account numbers that correspond to an account(s) at NSCC for purposes of permitting the Exchange to debit any undisputed or final fees, fines, charges, and/or other monetary sanctions or other monies due and owing to the Exchange or other charges pursuant to Rule 15.1, including the Exchange Fee Schedule thereto; Regulatory Transaction Fees pursuant to Rule 15.1(b); dues, assessments and other charges pursuant to Rule 2.9 to the extent the Exchange were to determine to charge such fees; and fines, sanctions and other charges pursuant to Chapter 8 of the Exchange Rules [5] which are due and owing to the Exchange (collectively ''Debit Amount''). The Exchange Fee Schedule specifies charges for transactions, routing and other services provided by the Exchange and certain fees that are collected by the Financial Industry Regulatory Authority (''FINRA''). Only the charges which require payment to the Exchange would be subject to direct debit. The Exchange does not currently charge fees for certain of the services listed on the Exchange Fee Schedule. The Exchange would entitle Rule 15.3 ''Collection of Exchange Fees and Other Claims and Billing Policy.''

As proposed, the Exchange will send a monthly electronic invoice by email to each Member, generally by the 7th business day of each month for the Debit Amount due to the Exchange for the prior month. The Exchange will also send files to NSCC each month by the 17th business day of each month to initiate the debit of the Debit Amount due to the Exchange as stated on the Member's invoice for the prior month.

The Exchange anticipates that NSCC will process the debits on the day it receives the file or the following business day. Because Members will be provided with an invoice approximately two weeks before the debit date, Members will have adequate time to contact Exchange staff with any questions concerning the invoice. If a Member disagrees with the invoice in whole or in part, the Exchange would not commence the debit for the disputed amount until the dispute is resolved. Specifically, the Exchange will not include the disputed amount (or the entire invoice if it is not feasible to identify the disputed amounts) in the NSCC debit amount if the Member has provided written notification of the dispute to the Finance Department of the Exchange by the later of the 16th business day of the month or ten days after the date the electronic invoice was sent to the Member, and the amount in dispute is at least $10,000 or greater.

Once NSCC receives the file from the Exchange, NSCC would proceed to debit the amounts indicated from the account of the Member that clears the applicable transactions (''Clearing Member'', *i.e.,* either a Member that is self-clearing or another Member that provides clearing services on behalf of the Member) and disburse such amounts to the Exchange. In the instance where the Member clears through another Member, the Exchange understands that the estimated transaction fees owed to the Exchange are typically debited by the Clearing Member on a daily basis using daily transaction detail reports provided by the Exchange to the Clearing Member in order to ensure adequate funds have been escrowed. The Exchange notes that it is proposing to permit a Member to designate one or more clearing account numbers that correspond to an account(s) at NSCC to permit Members that clear through multiple different clearing accounts to set up the billing process with the Exchange in a manner that is most efficient for internal reconciliation and billing purposes of the Member.

The Exchange believes that the proposed debiting process for Members would create an efficient method of collecting undisputed or final fees, fines, charges and/or other monetary sanctions or monies due and owing to the Exchange. An alternative process could cause collection matters to divert staff resources away from the Exchange's regulatory and business purposes. Moreover, the Exchange believes that it is reasonable to provide for a $10,000 limitation on pre-debit billing disputes since it would be inefficient to delay a direct debit for a de minimis amount. Members will still be able to dispute billing amounts that are less than $10,000 pursuant to paragraph (b) of Rule 15.3, as described below. The Exchange notes that a comparable debiting process is used by the Investors Exchange (''IEX''), the

[5] This includes, among other things, fines which result from disciplinary proceedings or actions taken pursuant to Chapter 8 of the Exchange Rules, as specified in Rule 8.1(a). In addition, the Exchange notes that it also has the authority under Rules 7.1(b) to report to the Chief Regulatory Officer (''CRO'') any Member who does not pay any dues, fees, assessments, charges or other amounts due to the Exchange within 90 days after the same has become payable and the CRO may, after giving reasonable notice to the Member of such arrearages, suspend the Member until payment is made. While this direct debit process should minimize failures to pay, those rules nevertheless will act as a backstop to the direct debit process. With respect to disciplinary proceedings, the Exchange would not debit any monies until such action is final. The Exchange would not consider an action final until all appeal periods have run and/or all appeal timeframes are exhausted. With respect to non-disciplinary actions, the Exchange would similarly not take action to debit a Member account until all appeal periods have run and/or all appeal timeframes are exhausted. Any uncontested disciplinary or non-disciplinary actions will be debited, and the amount due will appear on the Member's invoice prior to the actual NSCC debit.

Nasdaq Stock Market LLC (''Nasdaq''), Nasdaq BX, Inc. (''Nasdaq BX''), and Nasdaq PHLX LLC (''Nasdaq Phlx'').[6]

Billing Dispute Process

In addition to, and separate from the pre-debit dispute process described above, the Exchange also proposes to adopt a billing policy, pursuant to paragraph (b) of Rule 15.3, to require all pricing disputes, with respect to fees payable to the Exchange,[7] to be submitted to the Exchange in writing[8] and accompanied by supporting documentation within sixty days of receipt of an invoice. The Exchange believes that this policy will conserve Exchange resources, which are expended when untimely billing disputes require staff to research applicable fees and order information beyond two months after the invoice was issued. The sixty-day limitation would be applicable to all fees specified in paragraph (a) of Rule 15.3.

The Exchange expects that the proposed policy will provide a potential cost savings to the Exchange in that it would alleviate administrative burdens related to belated billing disputes, which could divert staff resources away from the Exchange's regulatory and business purposes. A similar policy is in place today at IEX, Nasdaq, Nasdaq BX, and Nasdaq Phlx.[9]

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,[10] in general, and furthers the objectives of Section 6(b)(5) of the Act,[11] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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. Specifically, the Exchange believes that the direct debit process will provide Members with an efficient process to pay undisputed or final fees, fines, charges and/or monetary sanctions or monies due and owing to the Exchange. Similarly, the billing policy will create an objective process and will be fair to Members. Further, both aspects of the proposal are expected to result in lower administrative costs for the Exchange.

The Exchange believes that the proposal to debit NSCC accounts is reasonable because it would ease the Member's administrative burden in paying monthly invoices, avoid overdue balances and provide efficient collection from all Members who owe monies to the Exchange. Moreover, the Exchange believes that the 10-day minimum time frame provided to Members to dispute invoices is reasonable and adequate to enable Members to identify potentially erroneous charges. In addition, the Exchange believes that the $10,000 limitation on pre-debit billing disputes is reasonable because it would be inefficient to delay a direct debit for a de minimis amount. Members will still be able to dispute billing amounts that are less than $10,000 pursuant to paragraph (b) of Rule 15.3.

Further, the Exchange believes that the requirement that billing disputes for specified fees be submitted to the Exchange within sixty days from receipt of the invoice will set objective standards, will be fair to Members, and that sixty days is ample time to review an invoice and dispute any pricing related to the transactions for that time period. It is also expected to lower the Exchange's administrative costs. An identical provision is applicable to IEX, Nasdaq, Nasdaq BX, and Nasdaq Phlx.[12]

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange believes its proposed rule change would not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The proposed debit process and billing policy would apply uniformly to all Members and will not disproportionately burden or otherwise impact any single Member.

The Exchange does not believe that the proposal will create an intermarket burden on competition since the Exchange will only debit fees (other than de minimis fees below $10,000) that are undisputed by the Member and Members will have a reasonable opportunity to dispute fees both before and after the direct debit process. The Exchange also does not believe that the proposal will create an intramarket burden on competition, since the proposed direct debit process and billing policy will be applied equally to all Members. Moreover, other exchanges use a comparable process which the Exchange believes is generally familiar to Members. Consequently, the Exchange does not believe that the proposal raises any new or novel issues that have not been previously considered by the Commission in connection with direct debit and billing policies of other exchanges.[13]

Further, this proposal is expected to provide a cost savings to the Exchange in that it would alleviate administrative processes related to the collection of monies owed to the Exchange by Members. Collection matters divert staff resources away from the Exchange's regulatory and business purposes. In addition, the debiting process would mitigate against Member accounts becoming overdue.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange neither solicited nor received comments on the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act[14] and Rule 19b–4(f)(6) thereunder.[15]

A proposed rule change filed pursuant to Rule 19b–4(f)(6) under the Act[16] normally does not become operative for 30 days after the date of its filing. However, Rule 19b–4(f)(6)(iii)[17] permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay. The Exchange believes that waiver of the operative delay is

[6] *See* IEX Rule 15.120, Nasdaq Rule Equity 7, Section 70, Nasdaq BX Rule Equity 7, Section 111, and Nasdaq Phlx Rule Equity 7, Section 2.

[7] Fees that are collected by FINRA would not be subject to the billing policy, and any disputes would need to be raised by the Member directly with FINRA.

[8] The Exchange invoice will specify the email address where billing disputes must be submitted.

[9] *See supra* note 6.

[10] 15 U.S.C. 78f(b).

[11] 15 U.S.C. 78f(b)(5).

[12] *See supra* note 6.

[13] *See supra* note 6.

[14] 15 U.S.C. 78s(b)(3)(A).

[15] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

[16] 17 CFR 240.19b–4(f)(6).

[17] 17 CFR 240.19b–4(f)(6)(iii).

consistent with the protection of investors and the public interest because it will allow the Exchange to provide a consistent process from the inception of the Exchange's operations for Members to pay undisputed or final fees, fines, charges and/or monetary sanctions or monies due and owing to the Exchange. The Commission believes that waiver of the 30-day operative delay is consistent with the protection of investors and the public interest because the proposed rule change does not raise any novel issues and is based on the rules of several other exchanges discussed above. Further, the proposal does not limit or relieve the Exchange from its responsibility to accurately assess fees and apply its fee schedule at all times. Therefore, the Commission hereby waives the operative delay and designates the proposal as operative upon filing.[18]

At any time within 60 days of the filing of the 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) [19] 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–MEMX–2020–06 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–MEMX–2020–06. 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–MEMX–2020–06 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[20]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20129 Filed 9–11–20; 8:45 am]

BILLING CODE 8011–01–P

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89777; File No. SR–CboeEDGX–2020–043]

Self-Regulatory Organizations; Cboe EDGX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Update Rule 13.4(a), Stating It Will Utilize MIAX PEARL Market Data From the CQSUQDF for Purposes of Order Handling, Routing, Execution, and Related Compliance Processes

September 8, 2020.

Pursuant to Section 19(b)(1) [1] of the Securities Exchange Act of 1934 (the "Act") [2] and Rule 19b–4 thereunder,[3] notice is hereby given that on August 25, 2020, Cboe EDGX Exchange, Inc. (the "Exchange" or "EDGX") filed with the Securities and Exchange Commission (the "Commission") the proposed rule change as described in Items I and II 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

Cboe EDGX Exchange, Inc. ("EDGX" or the "Exchange") proposes a rule change to Rule 13.4(a), stating it will utilize MIAX PEARL market data from the CQSUQDF for purposes of order handling, routing, execution, and related compliance processes. The text of the proposed rule change is provided in Exhibit 5.

The text of the proposed rule change is also available on the Exchange's website (*http://markets.cboe.com/us/options/regulation/rule_filings/edgx/*), at the Exchange's Office of the Secretary, 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to update Rule 13.4(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of the MIAX PEARL as an equities exchange.

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[18] For purposes only of waiving the 30-day operative delay, the Commission also has considered the proposed rule's impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[19] 15 U.S.C. 78s(b)(2)(B).

[20] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

On August 14, 2020, the Commission approved MIAX PEARL's proposed rule change to establish rules governing the trading of equities securities.[4] MIAX PEARL announced that it plans to launch equities trading on September 25, 2020.[5] The Exchange, therefore, proposes to update Rule 13.4(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of MIAX PEARL as an equities exchange beginning on September 25, 2020. Specifically, the Exchange proposes to amend Rule 13.4(a) to include MIAX PEARL by stating it will utilize MIAX PEARL market data from the Consolidated Quotation System (''CQS'')/UTP Quotation Data Feed (''UQDF'') for purposes of order handling, routing, execution, and related compliance processes. At this stage, no secondary source for MIAX PEARL market data will be used.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[6] in general, and furthers the objectives of Section 6(b)(5) of the Act,[7] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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.

The Exchange believes that its proposal to update Exchange Rule 13.4(a) to include MIAX PEARL will ensure that the Rule correctly identifies and publicly states on a market-by-market basis all of the specific network processor and proprietary data feeds that the Exchange utilizes for the handling, routing, and execution of orders, and for performing the regulatory compliance checks related to each of those functions. The proposed rule changes also remove impediments to and perfects the mechanism of a free and open market and protects investors and the public interest because it provides additional specificity, clarity and transparency.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange believes its proposed rule change would not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. To the contrary, the Exchange believes the proposal would enhance competition because including all of the exchanges enhances transparency and enables investors to better assess the quality of the Exchange's execution and routing services.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from Members or other interested parties.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

(i) Significantly affect the protection of investors or the public interest;

(ii) impose any significant burden on competition; and

(iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act[8] and Rule 19b–4(f)(6) thereunder.[9]

At any time within 60 days of the filing of the 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.

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–CboeEDGX–2020–043 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–CboeEDGX–2020–043. 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–CboeEDGX–2020–043 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[10]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20123 Filed 9–11–20; 8:45 am]

BILLING CODE 8011–01–P

[4] *See* Securities Exchange Act No. 89562 (August 14, 2020).

[5] *See supra* note 3 [sic].

[6] 15 U.S.C. 78f.

[7] 15 U.S.C. 78f(b)(5).

[8] 15 U.S.C. 78s(b)(3)(A).

[9] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has fulfilled this requirement.

[10] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89783; File No. SR–BX–2020–024]

Self-Regulatory Organizations; Nasdaq BX, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Rule 4759

September 8, 2020.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act''),[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on August 27, 2020, Nasdaq BX, Inc. (''BX'' or ''Exchange'') filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. 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 Rule 4759 (Data Feeds Utilized) to add the Long-Term Stock Exchange, Inc. (''LTSE''), MIAX PEARL, LLC (''MIAX PEARL'') and MEMX LLC (''MEMX'') to the list of market centers under Rule 4759 and provide that the Exchange will utilize CQS/UQDF.

The text of the proposed rule change is available on the Exchange's website at *https://listingcenter.nasdaq.com/rulebook/bx/rules,* 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 Exchange 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 these 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 aspects of such statements.

[1] 15 U.S.C. 78s(b)(1).

[2] 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

In anticipation of their planned launches [3] the Exchange proposes to amend the table in Rule 4759 to include LTSE, MIAX Pearl and MEMX. The Exchange will use securities information processor (''SIP'') data, *i.e.,* CQS SIP data, for securities reported under the Consolidated Quotation System and Consolidated Quotation Plan and UQDF SIP data for securities reported under the Nasdaq Unlisted Trading Privileges Plan to obtain LTSE, MIAX Pearl and MEMX quotation information for the handling, routing and execution of orders, as well as for the regulatory compliance processes related to those functions. At this stage, no secondary source for LTSE, MIAX Pearl or MEMX will be used.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,[4] in general, and furthers the objectives of Section 6(b)(5) of the Act,[5] in particular, in that it is designed to promote just and equitable principles of trade, to 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.

The Exchange believes that the proposed rule change removes impediments to and perfects the mechanism of a free and open market because adding LTSE, MIAX Pearl and MEMX because updating its list of market centers for which the Exchange consumes quotation data will provide clarity to market participants. Moreover, it is necessary and consistent with the public interest and the protection of investors to update the Exchange's table of market centers in order to provide transparency with respect to all the direct proprietary and network processor feeds from which the Exchange obtains market data. Additionally, a similar change has been proposed by other exchanges.[6]

[3] LTSE plans to begin phase-in of production securities on August, 28, 2020. *See* LTSE Market Announcement available at, *https://assets.ctfassets.net/cchj2z2dcfyd/rnGvgggJUplaIk6N1xNA7/41926d3925a177d6455868090c46aeda/MA-2020-020__Production_Securities_Launching_August_28__-_Google_Docs.pdf.* MIAX Pearl Equities will begin trading in September 2020, pending SEC approval. *See* MIAX Pearl Alerts available at, *https://www.miaxoptions.com/alerts/2020/02/14/miax-pearl-equities-exchange-codes-and-important-dates-regarding-launch-new.* MEMX is expected to launch on September 4, 2020. *See* MEMX Update from Jonathan Kellner, dated June 11, 2020, available at *https://memx.com/memx-update/.*

[4] 15 U.S.C. 78f(b).

[5] 15 U.S.C. 78f(b)(5).

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. The proposed rule change is not designed to address any competitive issue; instead, its purpose is to enhance transparency with respect to the operation of the Exchange and its use of market data feeds.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) Significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act [7] and Rule 19b–4(f)(6) thereunder.[8]

A proposed rule change filed pursuant to Rule 19b–4(f)(6) under the Act [9] normally does not become operative for 30 days after the date of its

[6] *See* Securities Exchange Act Release Nos. 88313 (March 3, 2020), 85 FR 13684 (March 9, 2020) (SR–IEX–2020–03); 88587 (April 8, 2020), 85 FR 20794 (April 14, 2020) (SR–NASDAQ–2020–015); 88601 (April 8, 2020), 85 FR 20798 (April 14, 2020) (SR–NYSE–2020–31); 88604 (April 8, 2020), 85 FR 20741 (April 14, 2020) (SR–NYSECHX–2020–12); 88610 (April 9, 2020), 85 FR 21033 (April 15, 2020) (SR–NYSEARCA–2020–30); 88611 (April 9, 2020), 85 FR 21047 (April 15, 2020) (SR–NYSENAT–2020–15); 89382 (July 23, 2020), 85 FR 45719 (July 29, 2020) (SR–NYSECHX–2020–22); 89369 (July 21, 2020), 85 FR 45270 (July 27, 2020) (SR–NYSE–2020–60); 89387(July 23, 2020), 85 FR 45722 (July 29, 2020) (SR–NYSEARCA–2020–67); 89388 (July 23, 2020), 85 FR 45711 (July 29, 2020) (SR–NYSENAT–2020–23); 89580 (August 17, 2020), 85 FR 51828 (August 21, 2020) (SR–IEX–2020–11).

[7] 15 U.S.C. 78s(b)(3)(A).

[8] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

[9] 17 CFR 240.19b–4(f)(6).

filing. However, Rule 19b–4(f)(6)(iii) [10] permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has requested that the Commission waive the 30-day operative delay. Waiver of the operative delay would allow the Exchange to disclose the updated list of market centers for which the Exchange consumes quotation data, and the source of the quotation data, at the time that LTSE, MIAX Pearl, and MEMX become operational. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest. Accordingly, the Commission waives the 30-day operative delay and designates the proposed rule change as operative upon filing.[11]

At any time within 60 days of the filing of the 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 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–BX–2020–024 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–BX–2020–024. 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–BX–2020–024 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[12]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20128 Filed 9–11–20; 8:45 am]

BILLING CODE 8011–01–P

[10] 17 CFR 240.19b–4(f)(6)(iii).

[11] For purposes only of waiving the 30-day operative delay, the Commission also has considered the proposed rule's impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[12] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–89779; File No. SR–CboeBZX–2020–068]

Self-Regulatory Organizations; Cboe BZX Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change To Update Rule 11.26(a), Stating It Will Utilize MIAX PEARL Market Data From the CQSUQDF for Purposes of Order Handling, Routing, Execution, and Related Compliance Processes

September 8, 2020.

Pursuant to Section 19(b)(1) [1] of the Securities Exchange Act of 1934 (the ''Act'') [2] and Rule 19b–4 thereunder,[3] notice is hereby given that on August 25, 2020, Cboe BZX Exchange, Inc. (the ''Exchange'' or ''BZX'') filed with the Securities and Exchange Commission (the ''Commission'') the proposed rule change as described in Items I and II 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

Cboe BZX Exchange, Inc. (''BZX'' or the ''Exchange'') proposes to update Rule 11.26(a), stating it will utilize MIAX PEARL market data from the CQSUQDF for purposes of order handling, routing, execution, and related compliance processes. The text of the proposed rule change is provided in Exhibit 5.

The text of the proposed rule change is also available on the Exchange's website (*http://markets.cboe.com/us/equities/regulation/rule_filings/bzx/*), at the Exchange's Office of the Secretary, 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 Exchange 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 these 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 aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to update Rule 11.26(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of the MIAX PEARL as an equities exchange.

On August 14, 2020, the Commission approved MIAX PEARL's proposed rule change to establish rules governing the

[1] 15 U.S.C. 78s(b)(1).

[2] 15 U.S.C. 78a.

[3] 17 CFR 240.19b–4.

trading of equities securities.[4] MIAX PEARL announced that it plans to launch equities trading on September 25, 2020.[5] The Exchange, therefore, proposes to update Rule 11.26(a) regarding the public disclosure of the sources of data that the Exchange utilizes when performing: (i) Order handling; (ii) order routing; (iii) order execution; and (iv) related compliance processes to reflect the operation of MIAX PEARL as an equities exchange beginning on September 25, 2020. Specifically, the Exchange proposes to amend Rule 11.26(a) to include MIAX PEARL by stating it will utilize MIAX PEARL market data from the Consolidated Quotation System (''CQS'')/UTP Quotation Data Feed (''UQDF'') for purposes of order handling, routing, execution, and related compliance processes. At this stage, no secondary source for MIAX PEARL market data will be used.

2. Statutory Basis

The Exchange believes that the proposed rule change is consistent with Section 6(b) of the Act,[6] in general, and furthers the objectives of Section 6(b)(5) of the Act,[7] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to 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.

The Exchange believes that its proposal to update Exchange Rule 11.26(a) to include MIAX PEARL will ensure that the Rule correctly identifies and publicly states on a market-by-market basis all of the specific network processor and proprietary data feeds that the Exchange utilizes for the handling, routing, and execution of orders, and for performing the regulatory compliance checks related to each of those functions. The proposed rule changes also remove impediments to and perfects the mechanism of a free and open market and protects investors and the public interest because it provides additional specificity, clarity and transparency.

[4] *See* Securities Exchange Act No. 89562 (August 14, 2020).

[5] *See supra* note 3 [sic].

[6] 15 U.S.C. 78f.

[7] 15 U.S.C. 78f(b)(5).

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange believes its proposed rule change would not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. To the contrary, the Exchange believes the proposal would enhance competition because including all of the exchanges enhances transparency and enables investors to better assess the quality of the Exchange's execution and routing services.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from Members or other interested parties.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not:

(i) Significantly affect the protection of investors or the public interest;

(ii) impose any significant burden on competition; and

(iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act[8] and Rule 19b–4(f)(6) thereunder.[9]

At any time within 60 days of the filing of the 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.

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:

[8] 15 U.S.C. 78s(b)(3)(A).

[9] 17 CFR 240.19b–4(f)(6). In addition, Rule 19b–4(f)(6)(iii) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has fulfilled this requirement.

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–CboeBZX–2020–068 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–CboeBZX–2020–068. 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–CboeBZX–2020–068 and should be submitted on or before October 5, 2020.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[10]

J. Matthew DeLesDernier,

Assistant Secretary.

[FR Doc. 2020–20125 Filed 9–11–20; 8:45 am]

BILLING CODE 8011–01–P

[10] 17 CFR 200.30–3(a)(12).

SMALL BUSINESS ADMINISTRATION

[Disaster Declaration #16643 and #16644; Louisiana Disaster Number LA–00104]

Presidential Declaration of a Major Disaster for Public Assistance Only for the State of Louisiana

AGENCY: U.S. Small Business Administration.

ACTION: Notice.

SUMMARY: This is a Notice of the Presidential declaration of a major disaster for Public Assistance Only for the State of Louisiana (FEMA–4559–DR), dated 09/05/2020.

Incident: Hurricane Laura.

Incident Period: 08/22/2020 through 08/27/2020.

DATES: Issued on 09/05/2020.

Physical Loan Application Deadline Date: 11/04/2020.

Economic Injury (EIDL) Loan Application Deadline Date: 06/07/2021.

ADDRESSES: Submit completed loan applications to: U.S. Small Business Administration, Processing and Disbursement Center, 14925 Kingsport Road, Fort Worth, TX 76155.

FOR FURTHER INFORMATION CONTACT: A. Escobar, Office of Disaster Assistance, U.S. Small Business Administration, 409 3rd Street SW, Suite 6050, Washington, DC 20416, (202) 205–6734.

SUPPLEMENTARY INFORMATION: Notice is hereby given that as a result of the President's major disaster declaration on 09/05/2020, Private Non-Profit organizations that provide essential services of a governmental nature may file disaster loan applications at the address listed above or other locally announced locations.

The following areas have been determined to be adversely affected by the disaster:

Primary Parishes: Allen, Beauregard, Calcasieu, Cameron, Jefferson Davis, Vernon.

The Interest Rates are:

	Percent
For Physical Damage:	
Non-Profit Organizations With Credit Available Elsewhere ...	2.750
Non-Profit Organizations Without Credit Available Elsewhere	2.750
For Economic Injury:	
Non-Profit Organizations Without Credit Available Elsewhere	2.750

The number assigned to this disaster for physical damage is 166438 and for economic injury is 166440.

(Catalog of Federal Domestic Assistance Number 59008)

Cynthia Pitts,

Acting Associate Administrator for Disaster Assistance.

[FR Doc. 2020–20106 Filed 9–11–20; 8:45 am]

BILLING CODE 8026–03–P

SMALL BUSINESS ADMINISTRATION

Disaster Declaration #16533 and #16534; Michigan Disaster Number MI–00084; Presidential Declaration Amendment of a Major Disaster for the State of Michigan

AGENCY: Small Business Administration.

ACTION: Disaster declaration; Amendment 1.

SUMMARY: This is an amendment of the Presidential declaration of a major disaster for the State of MICHIGAN (FEMA–4547–DRs), dated 07/09/2020.

Incident: Severe Storms and Flooding.

Incident Period: 05/16/2020 through 05/22/2020.

DATES: Issued on 09/08/2020.

Physical Loan Application Deadline Date: 09/30/2020.

Economic Injury (EIDL) Loan Application Deadline Date: 04/09/2021.

ADDRESSES: Submit completed loan applications to: U.S. Small Business Administration, Processing and Disbursement Center, 14925 Kingsport Road, Fort Worth, TX 76155.

FOR FURTHER INFORMATION CONTACT: A. Escobar, Office of Disaster Assistance, U.S. Small Business Administration, 409 3rd Street SW, Suite 6050, Washington, DC 20416, (202) 205–6734.

SUPPLEMENTARY INFORMATION: The notice of the President's major disaster declaration for the State of Michigan, dated 07/09/2020, is hereby amended to extend the deadline for filing applications for physical damages as a result of this disaster to 09/30/2020.

All other information in the original declaration remains unchanged.

(Catalog of Federal Domestic Assistance Number 59008)

Cynthia Pitts,

Acting Associate Administrator for Disaster Assistance.

[FR Doc. 2020–20107 Filed 9–11–20; 8:45 am]

BILLING CODE 8026–03–P

SOCIAL SECURITY ADMINISTRATION

[Docket No. SSA–2020–0050]

Notice of Senior Executive Service Performance Review Board Membership

AGENCY: Social Security Administration.

ACTION: Notice of Senior Executive Service Performance Review Board Membership.

Authority: Title 5, U.S. Code, 4314 (c)(4), requires that the appointment of Performance Review Board members be published in the **Federal Register** before service on said Board begins.

The following persons will serve on the Performance Review Board which oversees the evaluation of performance appraisals of Senior Executive Service members of the Social Security Administration:

Bonnie Doyle, Chair
Seth Binstock *
Kathryn Caldwell *
Stephen Evangelista
Florence Felix-Lawson *
Erik Hansen
Kishayra Lambert *
Joseph Lytle
Dan Parry
Van Roland

* New Member

Bonnie Doyle,

Assistant Deputy Commissioner for Human Resources.

[FR Doc. 2020–20176 Filed 9–11–20; 8:45 am]

BILLING CODE 4191–02–P

DEPARTMENT OF STATE

[Public Notice: 11201]

Cultural Property Advisory Committee; Additional Meeting Agenda Item

AGENCY: Department of State.

ACTION: Notice.

SUMMARY: The Department of State is issuing this Notice to add an agenda item for the next meeting of the Cultural Property Advisory Committee, which will be held on October 27–29, 2020.

DATES: *Meeting:* The Cultural Property Advisory Committee (CPAC) will meet October 27–29, 2020, 10:00 a.m. to 5:00 p.m. (EDT). CPAC will hold an open session on October 27, 2020, at 2:00 p.m. (EDT). It will last approximately one hour.

Comments: The Committee will review your written comment if it is received by October 13, 2020, at 11:59 p.m. (EDT). For further instructions on submission of comments and participation, please see the previous Notice at 85 FR 51542.

FOR FURTHER INFORMATION CONTACT: For general questions concerning the meeting, contact Allison Davis, Bureau of Educational and Cultural Affairs—Cultural Heritage Center, by phone (202–632–6305) or email (*culprop@state.gov*).

SUPPLEMENTARY INFORMATION: The October 27–29, 2020, meeting of the Cultural Property Advisory Committee was announced in 85 FR 51542. This Notice adds an additional agenda item for that meeting.

In accordance with the Convention on Cultural Property Implementation Act (19 U.S.C. 2601 *et seq.*) (''the Act''), the Assistant Secretary of State for Educational and Cultural Affairs calls a meeting of the Cultural Property Advisory Committee (''the Committee'') (19 U.S.C. 2605(e)(2)). The Act describes the Committee's responsibilities. A portion of this meeting will be closed to the public pursuant to 5 U.S.C. 552b(c)(9)(B) and 19 U.S.C. 2605(h).

Addition to Meeting Agenda: The Committee will review the proposed extension of the cultural property agreement with the Government of the Republic of Bolivia. As previously announced (85 FR 51542), the Committee also will review proposed extensions of cultural property agreements with the Government of the Hellenic Republic and the Government of Nigeria.

Open Session Participation: The Committee will hold an open session of the meeting to receive oral public comments on Tuesday, October 27, 2020, from 2:00 p.m. to approximately 3:00 p.m. (EDT). We have provided specific instructions on how to participate or observe the open session at *http://culturalheritage.state.gov*. Further information about this meeting, and how to participate, are included in the previous Notice at 85 FR 51542. Include ''Bolivia'' in the subject line.

Allison R. Davis,

Executive Director, CPAC, Bureau of Educational and Cultural Affairs, Department of State.

[FR Doc. 2020–20155 Filed 9–11–20; 8:45 am]

BILLING CODE 4710–05–P

DEPARTMENT OF STATE

September 14, 2020 [Public Notice: 11203]

Notice of Public Meeting of the U.S. President's Emergency Plan for AIDS Relief (PEPFAR) Scientific Advisory Board

SUMMARY: In accordance with the Federal Advisory Committee Act, the U.S. Department of State is hereby giving notice that the PEPFAR Scientific Advisory Board (SAB) will be holding a meeting utilizing virtual technology. The meeting will be open to the public; a public comment session will be held during the meeting. Pre-registration is required for both public participation and comment.

DATES: The meeting will be held on Wednesday, October 7, 2020, from approximately 10:00 a.m. to 3:00 p.m. (ET) and on Thursday, October 8, 2020 from approximately 9:00 a.m. to 2:00 p.m. (ET). This meeting will be conducted utilizing Cisco WebEx virtual technology.

Agenda: SAB members will be discussing the novel coronavirus (COVID–19) and its impact on people living with or at risk of HIV infection; new biomedical preventions products; PEPFAR 2020 plans, programs and performance; adolescents and children with HIV; and advanced HIV disease. The agenda will be posted on the SAB website at *www.state.gov/scientific-advisory-board-pepfar* and also shared with registered participants. Registered members of the public will be permitted to participate in a question and answer period following the meeting in accordance with the Chair's instructions

ADDRESSES: Individuals who wish to participate in the meeting and/or provide public comment should register by sending an email to *SolomonCD@state.gov* or directly at *https://forms.gle/XTrWnPQoQWJhadhJ6.* Individuals will be required to provide their name, organization, and email address to register not later than September 30, 2020. The WebEx site will be forwarded to individuals who register by that time, up to the capacity of the meeting. Individuals requiring reasonable accommodation should also make their request by that date. Requests made after that date will be considered but might not be able to be fulfilled.

FOR FURTHER INFORMATION CONTACT: Dr. Sara Klucking, Designated Federal Officer for the Board, Office of the U.S. Global AIDS Coordinator and Health Diplomacy at *KluckingSR@state.gov* or (202) 704–5598. Additional information can also be obtained by accessing the SAB's page on the PEPFAR site at *www.state.gov/scientific-advisory-board-pepfar.*

SUPPLEMENTARY INFORMATION: The Board is established under the general authority of the Secretary of State and the Department of State (''the Department'') as set forth in 22 U.S.C. 2656, and consistent with the Federal Advisory Committee Act, as amended (5 U.S.C. Appendix). The Board serves the U.S. Global AIDS Coordinator solely in an advisory capacity concerning scientific, implementation, and policy issues related to the global response to HIV/AIDS.

Zachary A. Parker,

Director, Office of Directives Management.

[FR Doc. 2020–20180 Filed 9–11–20; 8:45 am]

BILLING CODE 4710–10–P

DEPARTMENT OF STATE

[Public Notice: 11202]

Proposal To Extend Cultural Property Agreement Between the United States and Bolivia

AGENCY: Department of State.

ACTION: Public notice.

SUMMARY: Proposal to extend the *Memorandum of Understanding Concerning the Imposition of Import Restrictions on Categories of Archaeological Material from the Pre-Columbian Cultures and Certain Ethnological Material from the Colonial and Republican Periods of Bolivia.*

FOR FURTHER INFORMATION CONTACT: Allison Davis, Cultural Heritage Center, Bureau of Educational and Cultural Affairs: 202–632–6307; *culprop@state.gov*; include ''Bolivia'' in the subject line.

SUPPLEMENTARY INFORMATION: Pursuant to the authority vested in the Assistant Secretary of State for Educational and Cultural Affairs, and pursuant to 19 U.S.C. 2602(f)(1), an extension of the *Memorandum of Understanding Concerning the Imposition of Import Restrictions on Categories of Archaeological Material from the Pre-Columbian Cultures and Certain Ethnological Material from the Colonial and Republican Periods of Bolivia* is hereby proposed.

A copy of the Memorandum of Understanding, the Designated List of categories of material restricted from import into the United States, and related information can be found at the Cultural Heritage Center website: *http://culturalheritage.state.gov.*

Allison R. Davis,

Executive Director, CPAC, Bureau of Educational and Cultural Affairs, Department of State.

[FR Doc. 2020–20156 Filed 9–11–20; 8:45 am]

BILLING CODE 4710–05–P

DEPARTMENT OF STATE

[Public Notice 11198]

U.S. Advisory Commission on Public Diplomacy; Notice of Meeting

The U.S. Advisory Commission on Public Diplomacy (ACPD) will hold a virtual public meeting from 12:00 p.m. until 1:30 p.m., Wednesday, September 30, 2020. The meeting will focus on public diplomacy's role in countering state-sponsored disinformation, based on the forthcoming ACPD special report, ''Public Diplomacy and the New ''Old'' War: Countering State-Sponsored Disinformation.'' A panel of experts on the current complex information environment will discuss opportunities and challenges for PD practitioners in responding to state-sponsored malign influence operations—U.S. Ambassador (ret.) Bruce Wharton; James Pamment, Nonresident Scholar at the Carnegie Endowment for International Peace; and Graham Brookie, Director and Managing Editor of the Atlantic Council's Digital Forensic Research Lab.

This meeting is open to the public, including the media and members and staff of governmental and non-governmental organizations. To obtain the web conference link and password and to request reasonable accommodation, please email ACPD Program Assistant Kristy Zamary at *ZamaryKK@state.gov.* Please send any request for reasonable accommodation not later than September 23, 2020. Requests received after that date will be considered, but might not be possible to fulfill. Attendees should plan to enter the web conference waiting room by 11:50 a.m. to allow for a prompt start. Since 1948, the ACPD has been charged with appraising activities intended to understand, inform, and influence foreign publics and to increase the understanding of, and support for, these same activities. The ACPD conducts research that provides honest assessments of public diplomacy efforts, and disseminates findings through reports, white papers, and other publications. It also holds public symposiums that generate informed discussions on public diplomacy issues and events. The Commission reports to the President, Secretary of State, and Congress. The Office of the Under Secretary of State for Public Diplomacy and Public Affairs supports it.

For more information on the U.S. Advisory Commission on Public Diplomacy, please contact the Commission's Executive Director, Vivian S. Walker, at *WalkerVS@state.gov* or Senior Advisor, Shawn Baxter, at *BaxterGS@state.gov,* or please visit *https://www.state.gov/bureaus-offices/under-secretary-for-public-diplomacy-and-public-affairs/united-states-advisory-commission-on-public-diplomacy/.*

Vivian S. Walker,

Executive Director, U.S. Advisory Commission on Public Diplomacy, Department of State.

[FR Doc. 2020–20220 Filed 9–11–20; 8:45 am]

BILLING CODE 4710–45–P

DEPARTMENT OF STATE

[Delegation of Authority No. 488]

Delegation of the Functions and Authorities of Part II of the Maritime SAFE Act

By virtue of the authority vested in the Secretary of State, including Section 1 of the State Department Basic Authorities Act, as amended (22 U.S.C. 2651a), and to the extent authorized by law, I hereby delegate to the Assistant Secretary for Oceans and International Environmental and Scientific Affairs the functions and authorities vested in the Secretary of State by Part II of the Maritime SAFE Act, Public Law 116–92, codified at 16 U.S.C. 8031–8034.

The Secretary, Deputy Secretary, and the Under Secretary for Economic Growth, Energy, and the Environment may at any time exercise any authority or function delegated by this delegation of authority.

The authorities delegated herein may be re-delegated, to the extent authorized by law.

This delegation of authority does not revoke or otherwise affect any other delegation of authority currently in effect. Any act, executive order, regulation, or procedure subject to, or affected by, this delegation shall be deemed to be such act, executive order, regulation, or procedure as amended from time to time.

This document shall be published in the **Federal Register**.

Dated: August 17, 2020.

Michael R. Pompeo,

Secretary of State.

[FR Doc. 2020–20212 Filed 9–11–20; 8:45 am]

BILLING CODE 4710–09–P

DEPARTMENT OF STATE

[Public Notice: 11204]

Certification Related to Foreign Military Financing for Colombia Under Section 7045(b)(2)(b) of the Department of State, Foreign Operations, and Related Programs Appropriations Act, 2020

Pursuant to section 7045(b)(2)(B) of the Department of State, Foreign Operations, and Related Programs Appropriations Act, 2020 (Div. G, Pub. L. 116–94), I hereby certify that:

(i) The Special Jurisdiction for Peace and other judicial authorities are taking effective steps to hold accountable perpetrators of gross violations of human rights in a manner consistent with international law, including for command responsibility, and sentence them to deprivation of liberty;

(ii) the Government of Colombia is taking effective steps to prevent attacks against human-rights defenders and other civil-society activists, trade unionists, and journalists, and judicial authorities are prosecuting those responsible for such attacks; and

(iii) senior military officers responsible for ordering, committing, and covering up cases of false positives are being held accountable, including by removal from active duty, if found guilty through criminal or disciplinary proceedings.

This Certification shall be published in the **Federal Register** and shall be transmitted, along with the accompanying Memorandum of Justification, to Congress.

Dated August 18, 2020.

Stephen E. Biegun,

Deputy Secretary of State.

[FR Doc. 2020–20210 Filed 9–11–20; 8:45 am]

BILLING CODE 4710–29–P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

[DOT–OST–2019–XXXX]

Research, Engineering, and Development Advisory Committee (REDAC); Notice of Public Meeting

AGENCY: Federal Aviation Administration, Department of Transportation.

ACTION: Notice of public meeting.

SUMMARY: This notice announces a meeting of the Research, Engineering, and Development Advisory Committee (REDAC).

DATES: The meeting will be held on October 7, 2020, from 9:30am–4:30pm. EST.

Requests for accommodations to a disability must be received by September 13, 2020. Individuals requesting to speak during the meeting must submit a written copy of their remarks to DOT by September 13, 2020. Requests to submit written materials to be reviewed during the meeting must be received no later than September 13, 2020.

ADDRESSES: The meeting will be held virtually. Virtual attendance information will be provided upon registration. A detailed agenda will be available on the REDAC internet website at *http://www.faa.gov/go/redac* at least one week before the meeting, along with copies of the meeting minutes after the meeting.

FOR FURTHER INFORMATION CONTACT: Chinita Roundtree-Coleman, REDAC PM/Lead, FAA/U.S. Department of Transportation, at *chinita.roundtree-coleman@faa.gov* or (609) 485–7149. Any committee related request should be sent to the person listed in this section.

SUPPLEMENTARY INFORMATION:

I. Background

The Research, Engineering, and Development Advisory Committee was created under the Federal Advisory Committee Act (FACA), in accordance with Public Law 100–591 (1988) and Public Law 101–508 (1990) to provide advice and recommendations to the FAA Administrator in support of the Agency's Research and Development (R&D) portfolio.

II. Agenda

At the meeting, the agenda will cover the following topics:

- FAA Research and Development Plan
- Emergence of new entrant vehicles and operations into the National Airspace System

III. Public Participation

The US Department of Transportation is committed to providing equal access to this meeting for all participants. If you need alternative formats or services because of a disability, such as sign language, interpretation, or other ancillary aids, please contact the person listed in the **FOR FURTHER INFORMATION CONTACT** section.

There will be 45 minutes allotted for oral comments from members of the public joining the meeting. To accommodate as many speakers as possible, the time for each commenter may be limited. Individuals wishing to reserve speaking time during the meeting must submit a request at the time of registration, as well as the name, address, and organizational affiliation of the proposed speaker. If the number of registrants requesting to make statements is greater than can be reasonably accommodated during the meeting, the FAA may conduct a lottery to determine the speakers. Speakers are requested to submit a written copy of their prepared remarks for inclusion in the meeting records and for circulation to REDAC members before the deadline listed in the **DATES** section. All prepared remarks submitted on time will be accepted and considered as part of the meeting's record. Any member of the public may present a written statement to the committee at any time.

Issued in Washington, DC, this 8th day of September 2020.

Chinita Roundtree-Coleman,

REDAC PM/Lead, Federal Aviation Administration.

[FR Doc. 2020–20141 Filed 9–11–20; 8:45 am]

BILLING CODE 4910–9X–P

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

Aviation Rulemaking Advisory Committee (ARAC); Renewal

AGENCY: Federal Aviation Administration (FAA), Transportation (DOT).

ACTION: Notice of renewal.

SUMMARY: The FAA announces the charter renewal of the Aviation Rulemaking Advisory Committee (ARAC), a Federal Advisory Committee that works with industry and the public to improve the development of the FAA's regulations. This charter renewal will take effect on September 14, 2020, and will expire after 2 years unless otherwise renewed.

FOR FURTHER INFORMATION CONTACT: Thuy H. Cooper, Federal Aviation Administration, 800 Independence Avenue SW, Washington, DC 20591, telephone (202) 267–4715; fax (202) 267–5075; email *9-awa-arac@faa.gov.*

SUPPLEMENTARY INFORMATION: Pursuant to section 14(a)(2)(A) of the Federal Advisory Committee Act (Pub. L. 92–463), the FAA is giving notice of the charter renewal for the ARAC. The ARAC was established to provide advice and recommendations to FAA on regulatory matters. The ARAC is composed of representatives from member organizations and associations that represent the various aviation industry segments. The diversity of the Committee ensures the requisite range of views and expertise necessary to discharge its responsibilities. See the ARAC website for details on pending tasks at *http://www.faa.gov/regulations_policies/rulemaking/committees/documents/*.

Issued in Washington, DC, on September 9, 2020.

Brandon Roberts,

Executive Director, Office of Rulemaking.

[FR Doc. 2020–20163 Filed 9–11–20; 8:45 am]

BILLING CODE 4910–13–P

FEDERAL REGISTER

Vol. 85 Monday,

No. 178 September 14, 2020

Part II

Department of the Treasury

Internal Revenue Service

26 CFR Part 1

Limitation on Deduction for Business Interest Expense; Limitation on Deduction for Business Interest Expense; Allocation of Interest Expense by Passthrough Entities; Dividends Paid by Regulated Investment Companies; Application of Limitation on Deduction for Business Interest Expense to United States Shareholders of Controlled Foreign Corporations and to Foreign Persons With Effectively Connected Income; Final Rule and Proposed Rule

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 9905]

RIN 1545–BO73; RIN 1545–BP07

Limitation on Deduction for Business Interest Expense

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations providing guidance about the limitation on the deduction for business interest expense after amendment of the Internal Revenue Code (Code) by the provisions commonly known as the Tax Cuts and Jobs Act, which was enacted on December 22, 2017, and the Coronavirus Aid, Relief, and Economic Security Act, which was enacted on March 27, 2020. The regulations provide guidance to taxpayers on how to calculate the limitation, what constitutes interest for purposes of the limitation, which taxpayers and trades or businesses are subject to the limitation, and how the limitation applies in consolidated group, partnership, international, and other contexts.

DATES:

Effective date: The regulations are effective on November 13, 2020. Sections 1.163(j)–1 through 1.163(j)–11 are generally applicable to taxable years beginning on or after November 13, 2020.

Applicability dates: For dates of applicability, see §§ 1.163(j)–1(c), 1.163(j)–2(k), 1.163(j)–3(d), 1.163(j)–4(g), 1.163(j)–5(h), 1.163(j)–6(p), 1.163(j)–9(k), 1.163(j)–10(f), 1.163(j)–11(d), 1.263A–15(a), 1.381(c)(20)–1(d), 1.382–2(b)(3), 1.382–5(f), 1.382–6(h), 1.383–1(j), 1.446–3(j)(2), 1.469–11(a)(3) and (4), 1.1502–36(h)(2), 1.1502–99(d), and 1.1504–4(i).

Pursuant to section 7805(b)(7), taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may apply the rules set forth in §§ 1.163(j)–1 through 1.163(j)–11, in their entirety, to a taxable year beginning after December 31, 2017, and before November 13, 2020, so long as the taxpayers and their related parties consistently apply these rules, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1,469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–90, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year. However, see § 1.163(j)–1(c) for the applicability date rules relating to notional principal contracts and the interest anti-avoidance rule; see also part II(E)(2) (relating to notional principal contracts) and part II(E)(4) (relating to the interest anti-avoidance rule) of the Summary of Comments and Revisions section of this preamble.

Alternatively, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may rely on proposed §§ 1.163(j)–1 through 1.163(j)–11, which were issued in a notice of proposed rulemaking (REG–106089–18) and published on December 28, 2018, in the **Federal Register** (83 FR 67490), in their entirety, for a taxable year beginning after December 31, 2017, and before November 13, 2020, so long as the taxpayers and their related parties consistently apply proposed §§ 1.163(j)–1 through –11, and, if applicable, proposed §§ 1.263A–9, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.882–5, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year. Notwithstanding the preceding sentence, taxpayers applying the provisions in the notice of proposed rulemaking may apply § 1.163(j)–1(b)(1)(iii) in these final regulations for taxable years beginning after December 31, 2017.

With respect to § 1.382–2 and, if applicable, §§ 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of § 1.382–2), and with respect to § 1.382–5 and, if applicable, §§ 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of § 1.382–5), the regulations apply to testing dates and ownership changes, respectively, occurring on or after November 13, 2020.

Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of § 1.382–2 and, if applicable, §§ 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of § 1.382–2), and § 1.382–5 and, if applicable, §§ 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of § 1.382–5), to a testing date or an ownership change, respectively, that occurs in a taxable year beginning after December 31, 2017, and before November 13, 2020, so long as the taxpayers and their related parties consistently apply the rules of §§ 1.163(j)–1 through –11, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, and 1.383–1, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–90, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

Alternatively, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may rely on the rules of proposed § 1.382–2 and, if applicable, §§ 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of § 1.382–2), and § 1.382–5 and, if applicable, §§ 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of § 1.382–5), which were issued in a notice of proposed rulemaking (REG–106089–18) and published on December 28, 2018, in the **Federal Register** (83 FR 67490), with respect to a testing date or an ownership change, respectively, that occurs in a taxable year beginning after December 31, 2017, and before November 13, 2020, so long as the taxpayers and their related parties consistently apply the rules of proposed §§ 1.163(j)–1 through –11, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, and 1.383–1, and, if applicable, proposed §§ 1.263A–9, 1.381(c)(20)–1, 1.469–9, 1.469–11, 1.882–5, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–90, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year. As noted previously, taxpayers relying on the provisions in the notice of proposed rulemaking may apply § 1.163(j)–1(b)(1)(iii) in these final regulations for taxable years ending after December 31, 2017.

FOR FURTHER INFORMATION CONTACT: Concerning § 1.163(j)–1, § 1.163(j)–2, § 1.163(j)–3, § 1.163(j)–9, § 1.263A–9, or § 1.263A–15, Sophia Wang, (202) 317–4890 or Justin Grill, (202) 317–4850; concerning § 1.163(j)–4, § 1.163(j)–5, § 1.163(j)–10, § 1.163(j)–11, § 1.381(c)(20)–1, § 1.382–1, § 1.382–2, § 1.382–5, § 1.382–6, § 1.382–7, § 1.383–0, § 1.383–1, § 1.1502–13, § 1.1502–21, § 1.1502–36, § 1.1502–79, § 1.1502–90, § 1.1502–91, § 1.1502–95, § 1.1502–98, § 1.1502–99, or § 1.1504–4, Russell Jones, (202) 317–5357, John Lovelace, (202) 317–5363, Aglaia Ovtchinnikova, (202) 317–6975, or Marie C. Milnes-Vasquez, (202) 317–3181; concerning § 1.163(j)–6, § 1.469–9(b)(2), § 1.469–11, § 1.704–1, § 1.1362–3, § 1.1368–1, or

§ 1.1377–1, William Kostak, (202) 317–6852, Anthony McQuillen, (202) 317–5027, or Adrienne Mikolashek, (202) 317–5050; concerning § 1.163(j)–7, § 1.163(j)–8, or § 1.882–5, Azeka Abramoff, (202) 317–3800, Angela Holland, (202) 317–5474, or Steve Jensen, (202) 317–6938; concerning § 1.446–3, § 1.860C–2, RICs, REITs, REMICs, and the definition of the term ''interest'', Michael Chin, (202) 317–5846 (not toll-free numbers).

ADDRESSES: Submit electronic submissions to the Federal eRulemaking Portal at *http://www.regulations.gov* (indicate IRS and REG–106089–18) by following the online instructions for submitting comments. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) will publish for public availability any comment received to its public docket, whether submitted electronically or in hard copy. Send hard copy submissions to CC:PA:LPD:PR (REG–106089–18), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

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This document contains amendments to the Income Tax Regulations (26 CFR part 1) under section 163(j) of the Code. The final regulations reflect amendments to section 163(j) made by Public Law 115–97, 131 Stat. 2054 (December 22, 2017), commonly referred to as the Tax Cuts and Jobs Act (the TCJA) and the Coronavirus Aid, Relief, and Economic Security Act, Public Law 116–136 (2020) (the CARES Act). Section 13301(a) of the TCJA amended section 163(j) by removing prior section 163(j)(1) through (9) and adding section 163(j)(1) through (10) and significantly changed the limitation for deducting interest on certain indebtedness. The provisions of section 163(j) as amended by section 13301 of the TCJA are effective for tax years beginning after December 31, 2017. The CARES Act further amended section 163(j) by redesignating section 163(j)(10), as amended by the TCJA, as new section 163(j)(11), and adding a new section 163(j)(10) providing special rules for applying section 163(j) to taxable years beginning in 2019 or 2020. All references to ''old section 163(j)'' in this document are references to section 163(j) prior to amendment by the TCJA and the CARES Act, and all references to ''section 163(j)'' are references to section 163(j) as amended by the TCJA and the CARES Act.

Old section 163(j) generally disallowed a deduction for ''disqualified interest'' paid or accrued by a corporation in a taxable year if the payor's debt-to-equity ratio exceeded 1.5 to 1.0, and if the payor's net interest expense exceeded 50 percent of its adjusted taxable income. Disqualified interest included interest paid or accrued to (1) related parties when no Federal income tax was imposed with respect to such interest; (2) unrelated parties in certain instances in which a related party guaranteed the debt; or (3) certain real estate investment trusts (REIT). Interest amounts disallowed for any taxable year under old section 163(j) were treated as interest paid or accrued in the succeeding taxable year and could be carried forward indefinitely. In addition, any excess limitation, the excess of the taxpayer's net interest expense over 50 percent of its adjusted taxable income, could be carried forward three years. The interest limitation under old section 163(j) was designed to prevent a taxpayer from deducting interest from its U.S. taxable income without a corresponding inclusion in U.S. taxable income by the recipient, or to prevent the stripping of earnings from the U.S. tax system.

In contrast, section 163(j) now applies broadly to all business interest expense regardless of whether the related indebtedness is between related parties or incurred by a corporation, and regardless of the taxpayer's debt-to-equity ratio. Section 163(j) provides an entirely new limitation on the deduction for ''business interest expense'' of all taxpayers, including, for example, individuals, corporations, partnerships, S corporations, unless a specific exclusion applies under section 163(j). Although certain terms are used in both old section 163(j) and section 163(j), such as ''adjusted taxable income,'' such terms have been updated in the final regulations to reflect the new limitation under section 163(j).

Section 163(j) generally limits the amount of business interest expense that can be deducted in the current taxable year (also referred to in this preamble as the current year). Under section 163(j)(1), the amount allowed as a deduction for business interest expense is limited to the sum of (1) the taxpayer's business interest income for the taxable year; (2) 30 percent of the taxpayer's adjusted taxable income (ATI) for the taxable year (30 percent

ATI limitation); and (3) the taxpayer's floor plan financing interest expense for the taxable year. As further described later in this Background section, section 163(j)(10), as amended by the CARES Act, provides special rules relating to the 30 percent ATI limitation for taxable years beginning in 2019 or 2020. The section 163(j) limitation applies to all taxpayers, except for certain small businesses that meet the gross receipts test in section 448(c) and certain trades or businesses listed in section 163(j)(7).

Section 163(j)(2) provides that the amount of any business interest not allowed as a deduction for any taxable year as a result of the section 163(j) limitation is carried forward and treated as business interest paid or accrued in the next taxable year. In contrast to old section 163(j), section 163(j) does not allow the carryforward of any excess limitation.

Section 163(j)(3) provides that the section 163(j) limitation does not apply to a taxpayer, other than a tax shelter as described in section 448(a)(3), with average annual gross receipts of $25 million or less, determined under section 448(c) (including any adjustment for inflation under section 448(c)(4)). For taxpayers other than corporations or partnerships, section 163(j)(3) provides that the gross receipts test is determined for purposes of section 163(j) as if the taxpayer were a corporation or partnership.

Section 163(j)(4) provides special rules for applying section 163(j) in the case of partnerships and S corporations. Section 163(j)(4)(A) requires that the limitation on the deduction for business interest expense be applied at the partnership level, and that a partner's ATI be increased by the partner's share of the partnership's excess taxable income, as defined in section 163(j)(4)(C), but not by the partner's distributive share of the partnership's income, gain, deduction, or loss. Section 163(j)(4)(B)(i) provides that the amount of partnership business interest expense limited by section 163(j)(1) is carried forward at the partner level. Section 163(j)(4)(B)(ii) provides that excess business interest expense allocated to a partner and carried forward is available to be deducted in a subsequent year only if, and to the extent, the partnership allocates excess taxable income to the partner. As further described later in this Background section, section 163(j)(10)(A)(ii)(II), as amended by the CARES Act, provides a special rule for excess business interest expense allocated to a partner in a taxable year beginning in 2019. Section 163(j)(4)(B)(iii) provides basis adjustment rules for a partner that is allocated excess business interest expense. Section 163(j)(4)(D) provides that rules similar to the rules of section 163(j)(4)(A) and (C) apply to S corporations and S corporation shareholders.

Section 163(j)(5) and (6) defines ''business interest'' and ''business interest income,'' respectively, for purposes of section 163(j). Generally, these terms include interest expense and interest includible in gross income that is properly allocable to a trade or business (as defined in section 163(j)(7)) and do not include investment income or investment expense within the meaning of section 163(d). The legislative history states that ''a corporation has neither investment interest nor investment income within the meaning of section 163(d). Thus, interest income and interest expense of a corporation is properly allocable to a trade or business, unless such trade or business is otherwise explicitly excluded from the application of the provision.'' H. Rept. 115–466, at 386, fn. 688 (2017).

Under section 163(j)(7), the limitation on the deduction for business interest expense in section 163(j)(1) does not apply to certain trades or businesses (excepted trades or businesses). The excepted trades or businesses are the trade or business of providing services as an employee, electing real property businesses, electing farming businesses, and certain regulated utility businesses.

Section 163(j)(8) defines ATI as the taxable income of the taxpayer without regard to the following: Items not properly allocable to a trade or business; business interest and business interest income; net operating loss (NOL) deductions; and deductions for qualified business income under section 199A. ATI also generally excludes deductions for depreciation, amortization, and depletion with respect to taxable years beginning before January 1, 2022, and it includes other adjustments provided by the Secretary of the Treasury.

Section 163(j)(9) defines ''floor plan financing interest'' as interest paid or accrued on ''floor plan financing indebtedness.'' These provisions allow taxpayers incurring interest expense for the purpose of securing an inventory of motor vehicles held for sale or lease to deduct the full expense without regard to the section 163(j) limitation.

Under section 163(j)(10)(A)(i), the amount of business interest that is deductible under section 163(j)(1) for taxable years beginning in 2019 or 2020 is computed using 50 percent, rather than 30 percent, of the taxpayer's ATI for the taxable year (50 percent ATI limitation). A taxpayer may elect not to apply the 50 percent ATI limitation to any taxable year beginning in 2019 or 2020, and instead apply the 30 percent ATI limitation. The election must be made separately for each taxable year. Once the taxpayer makes the election, the election may not be revoked without the consent of the Secretary of the Treasury or his delegate. See section 163(j)(10)(A)(iii).

Sections 163(j)(10)(A)(ii)(I) and 163(j)(10)(A)(iii) provide that, in the case of a partnership, the 50 percent ATI limitation does not apply to partnerships for taxable years beginning in 2019, and the election to not apply the 50 percent ATI limitation may be made only for taxable years beginning in 2020. This election may be made only by the partnership and may not be revoked without the consent of the Secretary of the Treasury or his delegate. Under section 163(j)(10)(A)(ii)(II), however, a partner treats 50 percent of its allocable share of a partnership's excess business interest expense for 2019 as a business interest expense in the partner's first taxable year beginning in 2020 that is not subject to the section 163(j) limitation (50 percent EBIE rule). The remaining 50 percent of the partner's allocable share of the partnership's excess business interest expense remains subject to the section 163(j) limitation applicable to excess business interest expense carried forward at the partner level. A partner may elect out of the 50 percent EBIE rule.

Section 163(j)(10)(B)(i) allows a taxpayer to elect to use its ATI for the last taxable year beginning in 2019 for the taxpayer's ATI in determining the taxpayer's section 163(j) limitation for any taxable year beginning in 2020.

Section 163(j)(11) provides cross-references to provisions requiring that electing farming businesses and electing real property businesses excepted from the section 163(j) limitation use the alternative depreciation system (ADS), rather than the general depreciation system for certain types of property. The required use of ADS results in the inability of these electing trades or businesses to use the additional first-year depreciation deduction under section 168(k) for those types of property.

On December 28, 2018, the Treasury Department and the IRS (1) published proposed regulations under section 163(j) in a notice of proposed rulemaking (REG–106089–18) (proposed regulations) in the **Federal Register** (83 FR 67490), and (2) withdrew the notice of proposed rulemaking (1991–2 C.B. 1040) published in the **Federal Register** on June 18, 1991 (56 FR 27907) (as corrected by 56 FR 40285 (August 14, 1991)) to implement rules under old section 163(j) (1991 Proposed Regulations). The proposed regulations were issued following guidance announcing and describing regulations intended to be issued under section 163(j). See Notice 2018–28, 2018–16 I.R.B. 492.

A public hearing was held on February 27, 2019. The Treasury Department and the IRS received written comments responding to the notice of proposed rulemaking. Comments received before the final regulations were substantially developed, including all comments received on or before the deadline for comments on February 26, 2019, were carefully considered in developing the final regulations.

Copies of the comments received are available for public inspection at *http://www.regulations.gov* or upon request. After consideration of the comments received and the testimony at the public hearing, this Treasury decision adopts the proposed regulations as revised in response to such comments and testimony as described in the Summary of Comments and Explanation of Revisions section. The revisions are discussed in this preamble. Concurrently with the publication of the final regulations, the Treasury Department and the IRS are publishing in the Proposed Rule section of this edition of the **Federal Register** (RIN 1545–BO76) a notice of proposed rulemaking providing additional proposed regulations under section 163(j) (REG–107911–18) (Concurrent NPRM). The Concurrent NPRM includes proposed regulations relating to changes made to section 163(j) under the CARES Act.

On September 10, 2019, the Treasury Department and the IRS published proposed regulations under section 382(h) (REG–125710–18) in the **Federal Register** (84 FR 47455) (the September 2019 section 382 proposed regulations). The September 2019 section 382 proposed regulations included a rule to clarify that section 382 disallowed business interest carryforwards are not treated as recognized built-in losses (RBILs). No formal comments were received on this rule during the comment period for the September 2019 section 382 proposed regulations.

On April 10, 2020, the Treasury Department and the IRS released Revenue Procedure 2020–22, 2020–18 I.R.B. 745, to provide the time and manner of making a late election, or withdrawing an election under section 163(j)(7)(B) to be an electing real property trade or business, or under section 163(j)(7)(C) to be an electing farming business, for taxable years beginning in 2018, 2019, or 2020. Revenue Procedure 2020–22 also provides the time and manner of making or revoking elections provided by the CARES Act under section 163(j)(10) for taxable years beginning in 2019 or 2020. As described earlier in this Background section, these elections are: (1) To not apply the 50 percent ATI limitation under section 163(j)(10)(A)(iii); (2) to use the taxpayer's ATI for the last taxable year beginning in 2019 to calculate the taxpayer's section 163(j) limitation in 2020 under section 163(j)(10)(B); and (3) for a partner to elect out of the 50 percent EBIE rule under section 163(j)(10)(A)(ii)(II).

Summary of Comments and Explanation of Revisions

I. Overview

The Treasury Department and the IRS received approximately 120 written comments in response to the notice of proposed rulemaking. Most of the comments addressing the proposed regulations are summarized in this Summary of Comments and Explanation of Revisions section. However, comments merely summarizing or interpreting the proposed regulations or recommending statutory revisions generally are not discussed in this preamble. Additionally, comments outside the scope of this rulemaking are generally not addressed in this Summary of Comments and Explanation of Revisions section.

The Treasury Department and the IRS continue to study comments on certain issues related to section 163(j), including issues that are beyond the scope of the final regulations (or the Concurrent NPRM in the Proposed Rules section of this issue of the **Federal Register**), and may discuss those comments if future guidance on those issues is published.

The final regulations retain the same basic structure as the proposed regulations, with certain revisions.

II. Comments on and Changes to Proposed § 1.163(j)–1: Definitions

Section 1.163(j)–1 provides definitions of the terms used in the final regulations. The following discussion addresses comments relating to proposed § 1.163(j)–1.

A. Definition and Calculation of Adjusted Taxable Income (ATI)—Proposed § 1.163(j)–1(b)(1)

1. Taxable Income and Tentative Taxable Income

Consistent with section 163(j)(8), proposed § 1.163(j)–1(b)(1) defines ATI as the ''taxable income'' of the taxpayer for the taxable year, with certain specified adjustments. Thus, in calculating ATI, the proposed regulations begin with taxable income as the amount to which adjustments are made when calculating ATI. Proposed § 1.163(j)–1(b)(37)(i) generally provides that the term ''taxable income'' has the meaning provided in section 63, but for purposes of section 163(j), is computed without regard to the application of section 163(j) and the section 163(j) regulations. However, in some instances in the section 163(j) regulations the term ''taxable income'' is used to indicate the amount calculated under section 63 for purposes other than calculating ATI.

To prevent confusion from using the term ''taxable income'' in different contexts (in determining ATI, and for purposes other than determining ATI), the final regulations use a new term, ''tentative taxable income,'' to refer to the amount to which adjustments are made in calculating ATI. See § 1.163(j)–1(b)(43). Tentative taxable income is generally determined in the same manner as taxable income under section 63, but is computed without regard to the application of the section 163(j) limitation, and without regard to any disallowed business interest expense carryforwards. This definitional change avoids confusion with section 63 taxable income, avoids creating an iterative loop that takes into account the section 163(j) limitation, and ensures that disallowed business interest expense carryforwards are taken into account only once in testing business interest expense against the limitation.

Therefore, ''tentative taxable income'' is used in the final regulations and, where appropriate, in this Summary of Comments and Explanation of Provisions section, to describe the starting point for the calculation of ATI in the final regulations. See part II(G)(1) of this Summary of Comments and Explanation of Revisions section.

2. Adjustments to ATI for Amounts Incurred as Depreciation, Amortization, and Depletion

Section 163(j)(8)(A)(v) defines ATI as the taxable income of the taxpayer computed without regard to certain items, including any deduction allowable for depreciation, amortization, or depletion for taxable years beginning before January 1, 2022. Consistent with section 163(j)(8)(A)(v), proposed § 1.163(j)–1(b)(1)(i) requires an addback to taxable income of deductions for depreciation, amortization, and depletion for taxable years beginning before January 1, 2022. In general, section 263A requires certain taxpayers that manufacture or produce inventory to capitalize all direct costs and certain indirect costs into the basis of the property produced or acquired for resale. Depreciation, amortization or depletion that is capitalized into inventory under section 263A is recovered through cost of goods sold as an offset to gross receipts in computing gross income; cost of goods sold reduces the amount realized upon the sale of goods that is used to calculate gross income and is technically not a deduction that is applied against gross income in determining taxable income. See §§ 1.61–3(a) and 1.263A–1(e)(3)(ii)(I) and (J). Thus, proposed § 1.163(j)–1(b)(1)(iii) provides that depreciation, amortization, or depletion expense capitalized into inventory under section 263A is not a depreciation, amortization, or depletion deduction, that may be added back to taxable income in computing ATI. The preamble to the proposed regulations further noted that an amount that is incurred as depreciation, amortization, or depletion, but that is capitalized to inventory under section 263A and included in costs of goods sold, is not a deduction for depreciation, amortization, or depletion for purposes of section 163(j).

Many commenters raised questions and concerns regarding proposed § 1.163(j)–1(b)(1)(iii) and requested that the addback of deductions for depreciation, amortization, and depletion include any amount that is required to be capitalized into inventory under section 263A. First, commenters stated that the provision does not reflect congressional intent, which was to determine ATI using earnings before interest, tax, depreciation, and amortization (EBITDA) through taxable year 2021 and using earnings before interest and tax (EBIT) thereafter. Commenters noted that the proposed rule would eliminate this distinction for certain manufacturers or producers of property for sale. Commenters pointed out that capital-intensive businesses that manufacture or produce inventory are at a disadvantage in comparison to other types of businesses because the manufacturers or producers would have to compute ATI without an addback for a substantial amount of their depreciation, and that neither section 163(j) nor its legislative history indicates an intent by Congress to treat manufacturers or producers of inventory differently from other trades or businesses. Commenters also contrasted the language in section 163(j)(8)(A)(iv), which allows an addback of ''the amount of any deduction *allowed* under section 199A,'' with section 163(j)(8)(A)(v), which allows an addback of ''any deduction *allowable* for depreciation, amortization, or depletion'' (emphasis added).

The phrase ''allowed or allowable'' is used in other Code provisions. Section 1016(a)(2) provides that, in calculating tax basis, adjustments are required for depreciation to the extent such amounts are allowed as deductions in computing taxable income but not less than the amounts allowable. Some commenters noted that depreciation allowable as a deduction for purposes of section 1016(a)(2) should be read consistently with depreciation allowable as a deduction for purposes of section 163(j), and that section 1016(a)(2) treats depreciation capitalized into inventory under section 263A as deductions allowable. As provided in section 263A(a)(2) and § 1.263A–1(c)(2), an amount is not subject to capitalization under section 263A unless such cost may be taken into account in computing taxable income.

The Treasury Department and the IRS have reconsidered proposed § 1.163(j)–1(b)(1)(iii). Accordingly, under the final regulations, the amount of any depreciation, amortization, or depletion that is capitalized into inventory under section 263A during taxable years beginning before January 1, 2022, is added back to tentative taxable income as a deduction for depreciation, amortization, or depletion when calculating ATI for that taxable year, regardless of the period in which the capitalized amount is recovered through cost of goods sold. For example, if a taxpayer capitalized an amount of depreciation to inventory under section 263A in the 2020 taxable year, but the inventory is not sold until the 2021 taxable year, the entire capitalized amount of depreciation is added back to tentative taxable income in the 2020 taxable year, and such capitalized amount of depreciation is not added back to tentative taxable income when the inventory is sold and recovered through cost of goods sold in the 2021 taxable year. Under such facts, the entire capitalized amount is deemed to be included in the calculation of the taxpayer's tentative taxable income for the 2020 taxable year, regardless of the period in which the capitalized amount is actually recovered. See §§ 1.163(j)–1(b)(1)(iii) and 1.163(j)–2(h)(3).

Further, in order to treat similarly situated taxpayers similarly, the final regulations allow taxpayers, and their related parties within the meaning of sections 267(b) and 707(b)(1), otherwise relying on the proposed regulations in their entirety under § 1.163(j)–1(c) to alternatively choose to follow § 1.163(j)–1(b)(1)(iii) rather than proposed § 1.163(j)–1(b)(1)(iii). See § 1.163(j)–1(c).

The Treasury Department and the IRS note that neither proposed § 1.163(j)–1(b)(1) nor § 1.163(j)–1(b)(1) determines the amount of allowed or allowable depreciation, amortization, or depletion for purposes of any other Code section (for example, sections 167(c), 1016(a)(2), 1245, and 1250). Accordingly, no inference should be drawn regarding the determination of the amount of allowed or allowable depreciation, amortization, or depletion under any other Code section based on proposed § 1.163(j)–1(b)(1) or § 1.163(j)–1(b)(1).

In addition to comments about whether depreciation, amortization, and depletion include amounts recovered through cost of goods sold, a commenter requested clarification that section 179 deductions are depreciation deductions for purposes of section 163(j)(8)(A)(v) and proposed § 1.163(j)–1(b)(1)(i)(D). Section 179 deductions are allowed to be added back as amortization under proposed § 1.163(j)–1(b)(1)(i)(E), which allows an addback of any deduction for the amortization of intangibles (for example, under section 167 or 197) and other amortized expenditures (for example, under section 195(b)(1)(B), 248, or 1245(a)(2)(C)), for taxable years beginning before January 1, 2022. Section 1245(a)(2)(C) provides ''any deduction allowable under sections 179, 179B, 179C, 179D, 179E, 181, 190, 193, or 194 shall be treated as if it were a deduction allowable for amortization.'' Because section 179 deductions are included as amortization under proposed § 1.163(j)–1(b)(1)(i)(E), rather than as depreciation under proposed § 1.163(j)–1(b)(1)(i)(D), no clarification is necessary in the final regulations. See § 1.163(j)–1(b)(1)(i)(E).

3. ATI and Floor Plan Financing Interest

Consistent with section 163(j)(8)(A)(ii), the proposed regulations provide that any business interest expense or business interest income is added back to (in the case of business interest expense) or subtracted from (in the case of business interest income) taxable income in computing ATI. Because business interest expense includes floor plan financing interest expense, ATI is further adjusted by subtracting from it any floor plan financing interest expense under proposed § 1.163(j)–1(b)(1)(ii)(B). Floor plan financing interest expense is also separately included in the section 163(j) limitation as provided in section 163(j)(1)(C).

One commenter suggested that floor plan financing interest expense should not be subtracted from ATI because such adjustment is inconsistent with the statute and the ordering implied by section 168(k)(9)(B). The addition of floor plan financing interest expense as business interest in the calculation of ATI is consistent with section 163(j)(8)(A)(ii). The purpose of subtracting floor plan financing interest expense from tentative taxable income to compute ATI is to avoid the double benefit that would result upon separately including floor plan financing interest expense in the computation of the section 163(j) limitation. If floor plan financing interest expense were included in ATI without a corresponding subtraction, thus resulting in an increased ATI, taxpayers with such expense would be able to increase their section 163(j) limitation not only by the separately stated floor plan financing interest under section 163(j)(1)(C), but also by the inclusion of such amount in ATI, which would permit a deduction of $1.30 (or $1.50, if the 50 percent ATI limitation is applicable) of business interest expense for each $1 of floor plan financing interest expense. Although it is clear that Congress did not intend to limit the deduction for floor plan financing interest expense under section 163(j), there is no indication that Congress also intended to provide the additional benefit of an increased ATI related to floor plan financing interest expense. Therefore, under the authority granted in section 163(j)(8)(B), the final regulations adopt the proposed rule without change to include a subtraction of floor plan financing interest expense from tentative taxable income in computing ATI.

Several commenters also requested clarification and submitted recommendations on the interaction between section 168(k)(9) and section 163(j). Section 168(k)(9)(B) provides that the additional first-year depreciation deduction is not allowed for any property used in a trade or business that has had floor plan financing indebtedness (as defined in section 163(j)(9)), if the floor plan financing interest related to such indebtedness was taken into account under section 163(j)(1)(C).

First, commenters requested that floor plan financing indebtedness not be treated as taken into account if the sum of business interest income and 30 percent of ATI (the sum of section 163(j)(1)(A) and section 163(j)(1)(B)) is greater than the business interest expense paid or accrued in the taxable year. Second, if the sum of business interest income and 30 percent of ATI is less than the business interest expense paid or accrued in the taxable year, commenters requested that taxpayers be given the option to either include floor plan financing interest to increase the section 163(j) limitation, or to forgo the use of floor plan financing interest to increase the section 163(j) limitation (any forgone floor plan financing interest would be included in the disallowed business interest expense carryforward under proposed § 1.163(j)–2(c)) in order to utilize the additional first-year depreciation deduction under section 168(k).

Section 163(j) does not provide any guidance on the availability of section 168(k) for taxpayers that have had floor plan financing interest expense. As these comments relate to the operation of section 168(k)(9), taxpayers should look to Treasury Department or IRS guidance provided under section 168(k) for clarification. On September 24, 2019, the Treasury Department and the IRS published in the **Federal Register** final regulations (TD 9874, 84 FR 50108) and proposed regulations (REG–106808–19, 84 FR 50152) under section 168(k). The rules regarding when floor plan financing interest expense is ''taken into account'' for purposes of 168(k) are in the proposed regulations under § 1.168(k)–2(b)(2)(ii)(G). Accordingly, these final regulations do not address the interaction between section 163(j) and section 168(k)(9) regarding floor plan financing interest expense.

4. Adjustments to Taxable Income in Computing ATI Under Section 163(j)(8)(A)

Section 163(j)(8)(A) provides that ATI means taxable income ''computed without regard to'' the specified adjustments. The purpose of the adjustments listed in section 163(j)(8)(A) is to keep certain items, such as deductions for depreciation, amortization, depletion, or NOL carryforward amounts, from directly increasing or decreasing the amount of the deduction for business interest expense. Therefore, the Treasury Department and the IRS have determined that the adjustments listed in section 163(j)(8)(A) should adjust tentative taxable income for purposes of calculating ATI under § 1.163(j)–1(b)(1) only to the extent that they have been reflected (or deemed reflected, as in the case of certain amounts capitalized into inventory under section 263A as discussed in part II(A)(2) of this Summary of Comments and Explanation of Revisions section) in tentative taxable income under § 1.163(j)–1(b)(43).

A commenter requested that the definition of ATI not include some of the adjustments listed in section 163(j)(8)(A), such as the adjustments for NOL deductions and deductions under section 199A. The Treasury Department and the IRS do not have authority to ignore these clear and unambiguous statutory adjustments. Thus, the final regulations do not incorporate the commenter's suggestion.

5. Certain Adjustments to Tentative Taxable Income in Computing ATI Under Section 163(j)(8)(B)

Under the authority granted in section 163(j)(8)(B), the proposed regulations include several adjustments to taxable income in computing ATI to address certain sales or other dispositions of depreciable property, stock of a consolidated group member, or interests in a partnership. Proposed § 1.163(j)–1(b)(1)(ii)(C) provides that, if property is sold or otherwise disposed of, the lesser of the amount of gain on the disposition or the amount of depreciation, amortization, or depletion deductions (collectively, depreciation deductions) with respect to the property for the taxable years beginning after December 31, 2017 and before January 1, 2022 (such years, the EBITDA period) is subtracted from taxable income to determine ATI. Proposed § 1.163(j)–1(b)(1)(ii)(D) provides that, with respect to the sale or other disposition of stock of a member of a consolidated group that includes the selling member, the investment adjustments (see § 1.1502–32) with respect to such stock that are attributable to deductions described in proposed § 1.163(j)–1(b)(1)(ii)(C) are subtracted from taxable income. In turn, proposed § 1.163(j)–1(b)(1)(ii)(E) provides that, with respect to the sale or other disposition of an interest in a partnership, the taxpayer's distributive share of deductions described in proposed § 1.163(j)–1(b)(1)(ii)(C) with respect to property held by the partnership at the time of such disposition is subtracted from taxable income to the extent such deductions were allowable under section 704(d).

In general, when a taxpayer takes depreciation deductions with respect to an asset, the taxpayer must reduce its adjusted basis in the asset accordingly. As a result, the taxpayer will realize additional gain (or less loss) upon the subsequent disposition of the asset than the taxpayer would have realized absent depreciation deductions. Thus, except with regard to timing (and, in some cases, character), depreciation deductions should have no net effect on a taxpayer's taxable income.

In order to mitigate the effects of the section 163(j) limitation during the EBITDA period, Congress provided an adjustment to taxable income for depreciation deductions. More specifically, as discussed in part II(A)(2) of this Summary of Comments and Explanation of Revisions section, depreciation deductions are added back to taxable income during the EBITDA period, thereby increasing a taxpayer's ATI and its section 163(j) limitation. Congress intended this adjustment to be a timing provision that delays the inclusion of depreciation deductions in calculating a taxpayer's section 163(j) limitation. Stated differently, Congress intended to allow taxpayers to accelerate the recognition of gain attributable to depreciation deductions when computing ATI.

However, if a taxpayer were to sell its depreciable property after making the foregoing adjustment to ATI, the taxpayer would realize additional gain (or less loss) on the disposition as a result of its depreciation deductions, and the taxpayer's ATI would be increased yet again. Similarly, if the depreciable property were held by a member of a consolidated group (S), and if another member of the group were to sell S's stock after making negative adjustments to its basis in S's stock under § 1.1502–32 to reflect S's depreciation deductions, the consolidated group's ATI would be increased yet again. A similar double benefit would arise with respect to interests in a partnership if, after the partner's basis in its partnership interest is reduced by depreciation deductions associated with the depreciable property, ATI were to reflect that reduced basis upon a subsequent sale of the partnership interest.

Proposed § 1.163(j)–1(b)(1)(ii)(C), (D), and (E) were intended to address these situations and ensure that the positive adjustment for depreciation deductions during the EBITDA period merely defers (rather than permanently excludes) depreciation deductions from a taxpayer's calculation of the section 163(j) limitation.

Commenters submitted various questions and comments about these provisions. First, a commenter questioned whether these proposed subtractions from taxable income are an advisable exercise of the authority granted in section 163(j)(8)(B) in light of congressional silence on the issue. However, the 1991 Proposed Regulations contained similar subtractions from taxable income in computing ATI. The 1991 Proposed Regulations had been outstanding for more than 25 years when Congress enacted the TCJA. Thus, Congress likely was well aware of these adjustments when it granted the Secretary of the Treasury the authority to make adjustments in new section 163(j)(8)(B). Moreover, there is no indication that Congress intended to preclude the Secretary from making adjustments similar to those in the 1991 Proposed Regulations.

Second, commenters asked why the subtraction from taxable income in proposed § 1.163(j)–1(b)(1)(ii)(D) does not include a ''lesser of'' calculation similar to proposed § 1.163(j)–1(b)(1)(ii)(C), and they questioned whether the ''lesser of'' calculation in proposed § 1.163(j)–1(b)(1)(ii)(C) captures the correct amount. For example, if a taxpayer purchased property for $100x, fully depreciated the property, and then sold the property for $60x, should the amount that is backed out under proposed § 1.163(j)–1(b)(1)(ii)(C) be $60x or $100x? Commenters also stated that the presence of a ''lesser of'' limitation in proposed § 1.163(j)–1(b)(1)(ii)(C) and the absence of such a limitation in proposed § 1.163(j)–1(b)(1)(ii)(D) can yield discontinuities. For example, if S (a member of P's consolidated group) uses $50x to purchase an asset that it fully depreciates under section 168(k) (resulting in a $50x reduction in P's basis in its S stock under § 1.1502–32), and if S sells the depreciated asset for $25x the following year, the P group would have to subtract $25x from taxable income under proposed § 1.163(j)–1(b)(1)(ii)(C), whereas the group would have had to reduce its taxable income by $50x under proposed § 1.163(j)–1(b)(1)(ii)(D) if P had sold its S stock instead. Commenters recommended several solutions to address this discontinuity, including eliminating the ''lesser of'' test.

Proposed § 1.163(j)–1(b)(1)(ii)(D) does not include a ''lesser of'' calculation because such a calculation would require consolidated groups to value their assets each time there is a sale of member stock. However, the Treasury Department and the IRS recognize the discrepancy in taxable income adjustments between asset dispositions and member stock dispositions under the proposed regulations. To eliminate this discrepancy, the final regulations revise proposed § 1.163(j)–1(b)(1)(ii)(C) by eliminating the ''lesser of'' standard and requiring taxpayers to back out depreciation deductions that were allowed or allowable during the EBITDA period with respect to sales or dispositions of property. This revised approach is consistent with the adjustment for asset sales in the 1991 Proposed Regulations, is simpler for taxpayers to administer than the ''lesser of'' approach in the proposed regulations, and renders moot questions as to whether that ''lesser of'' calculation captures the correct amount. However, the Treasury Department and the IRS also recognize that, in certain cases, a ''lesser of'' computation would not be difficult to administer. Thus, the Concurrent NPRM provides taxpayers the option to apply the ''lesser of'' standard, so long as they do so consistently. See proposed § 1.163(j)–1(b)(1)(iv)(E) of the Concurrent NPRM.

Third, commenters asked whether the application of proposed § 1.163(j)–1(b)(1)(ii)(C) and (D) to the same consolidated group member would result in an inappropriate double inclusion if the asset sale precedes the stock sale, and whether proposed § 1.163(j)–1(b)(1)(ii)(C) should continue to apply to a group member if the sale of member stock precedes the asset sale. For example, S (a member of P's consolidated group) takes a $50x depreciation deduction in 2020 with respect to asset X, P's basis in its S stock is reduced accordingly under § 1.1502–32, and $50x is added back to the P group's tentative taxable income in computing its 2020 ATI. In 2021, S realizes a $50x gain upon the sale of asset X, P's basis in its S stock is increased accordingly by $50x under § 1.1502–32, and the P group subtracts $50x from its tentative taxable income under proposed § 1.163(j)–1(b)(1)(ii)(C) in computing its 2021 ATI. Then, in 2022, P sells the S stock to an unrelated buyer. Must P subtract another $50x from its tentative taxable income under proposed § 1.163(j)–1(b)(1)(ii)(D)? What if the order of sales were reversed (with P selling its S stock to a member of another consolidated group in 2021 and S selling asset X in 2022)—would both consolidated groups be required to subtract $50x from tentative taxable income in computing ATI? To prevent duplicative adjustments under proposed § 1.163(j)–1(b)(1)(ii)(C) and (D), commenters recommended that these rules ''turn off'' further subtractions once a subtraction already has been made under either provision, and that the application of proposed § 1.163(j)–1(b)(1)(ii)(C) be limited to the group in which the depreciation deductions accrued.

The Treasury Department and the IRS agree that the application of § 1.163(j)–1(b)(1)(ii)(C) and (D) to the same consolidated group member would result in an inappropriate double inclusion, and that proposed § 1.163(j)–1(b)(1)(ii)(C) should not apply to a former group member with respect to depreciation deductions claimed by the member in a former group. Thus, § 1.163(j)–1(b)(1)(iv)(D) provides anti-duplication rules to ensure that neither § 1.163(j)–1(b)(1)(ii)(C) nor § 1.163(j)–1(b)(1)(ii)(D) applies if a subtraction for the same economic amount already has been required under either provision.

For example, assume that P wholly owns S1, which wholly owns S2, which owns depreciable asset Q, and that S1 and S2 are members of P's consolidated group. Further assume that S2's depreciation deductions with respect to asset Q have resulted in investment adjustments in S1's stock in S2 and in P's stock in S1. If S1 were to sell its S2 stock to a third party, adjustments to the P group's tentative taxable income would be required under proposed § 1.163(j)–1(b)(1)(ii)(D). If P later were to sell its S1 stock to a third party, an additional adjustment under proposed § 1.163(j)–1(b)(1)(ii)(D) would not be required with respect to investment adjustments attributable to asset Q.

Fourth, commenters observed that these proposed subtractions from taxable income in computing ATI are required even if the disposition of the depreciable property, member stock, or partnership interest occurs many years after the EBITDA period. Commenters expressed concern that tracking depreciation deductions for purposes of these adjustments could become burdensome, and a commenter questioned the appropriateness in proposed § 1.163(j)–1(b)(1)(ii)(C) of treating all gain upon the disposition of property after the EBITDA period as attributable to depreciation deductions during the EBITDA period.

Commenters are correct in observing that these proposed adjustments to taxable income in computing ATI must be made even if the relevant depreciable asset, member stock, or partnership interest is disposed of after the EBITDA period. However, the Treasury Department and the IRS note that members of consolidated groups already must track depreciation deductions to calculate separate taxable income (see § 1.1502–12) and to preserve the location of tax items (see § 1.1502–13). Additionally, all taxpayers must track depreciation deductions on an asset-by-asset basis for purposes of section 1245. Thus, the Treasury Department and the IRS have determined that the adjustments proposed in § 1.163(j)–1(b)(1)(ii)(C), (D), and (E) should not impose a significant administrative burden in many situations. The Treasury Department and the IRS further note that eliminating the ''lesser of'' standard in proposed § 1.163(j)–1(b)(1)(ii)(C) (see the response to the second comment in this part of the Summary of Comments and Explanation of Revisions section) will render moot the commenter's concern about the calculation of gain.

Fifth, a commenter asked whether the term ''sale or other disposition'' in proposed § 1.163(j)–1(b)(1)(ii)(C), (D), and (E) is intended to apply to the transfer of stock of a consolidated group member in an intercompany transaction (within the meaning of § 1.1502–13(b)(1)(i)) or to the transfer of assets in a nonrecognition transaction to which section 381 applies (a section 381 transaction).

As provided in proposed § 1.163(j)–4(d)(2), a consolidated group has a single section 163(j) limitation, and intercompany items and corresponding items are disregarded for purposes of calculating the group's ATI to the extent they offset in amount. The Treasury Department and the IRS have determined that regarding intercompany items and corresponding items for purposes of § 1.163(j)–1(b)(1)(ii)(C) and (D) would be inconsistent with this general approach. Thus, § 1.163(j)–1(b)(1)(iv)(A)(*2*) provides that an intercompany transaction should not be treated as a ''sale or other disposition'' for purposes of § 1.163(j)–1(b)(1)(ii)(C) and (D).

In turn, the transfer of depreciable assets in a section 381 transaction generally should not be treated as a ''sale or other disposition'' because the transfer does not affect ATI and because the transferee corporation is the successor to the transferor corporation. Thus, the final regulations generally provide that a transfer of an asset to an acquiring corporation in a transaction to which section 381(a) applies is not treated as a ''sale or other disposition'' for purposes of § 1.163(j)–1(b)(1)(ii)(C), (D), and (E). However, if a member leaves a consolidated group, that transaction generally is treated as a sale or other disposition under the final regulations for purposes of § 1.163(j)–1(b)(1)(ii)(C) and (D), regardless of whether the transaction is a section 381 transaction, because the adjustment to ATI under these provisions should be reflected on the tax return of the group that received the benefit of the earlier increase in ATI.

Sixth, a commenter asked for clarification as to when the adjustment in proposed § 1.163(j)–1(b)(1)(ii)(D) is required and which investment adjustments under § 1.1502–32 are treated as ''attributable to'' depreciation deductions for purposes of this provision. For example, P wholly and directly owns both S and S1 (members of P's consolidated group). In 2021, S purchases asset X for \$100x and fully depreciates asset X under section 168(k), and P reduces its basis in its S stock by \$100x under § 1.1502–32. In 2022, P contributes the stock of S to S1 in an intercompany transaction (which, as noted previously, is not treated as a ''sale or other disposition'' for purposes of proposed § 1.163(j)–1(b)(1)(ii)(C) and (D)). If P later sells the S1 stock, is the adjustment in proposed § 1.163(j)–1(b)(1)(ii)(D) required even though no adjustment to P's basis in the S1 stock under § 1.1502–32 is ''attributable to'' the \$100x of depreciation deductions taken with respect to asset X?

The Treasury Department and the IRS have determined that the adjustment to tentative taxable income in proposed § 1.163(j)–1(b)(1)(ii)(D) should apply in the foregoing situation. The final regulations have been revised to provide that, for these purposes, P's stock in S1 would be treated as a successor asset (within the meaning of § 1.1502–13(j)(1)) to P's stock in S.

Seventh, commenters stated that there should be no adjustments to taxable income under proposed § 1.163(j)–1(b)(1)(ii)(C), (D), and (E) if and to the extent that adding back depreciation deductions pursuant to section 163(j)(8)(A)(v) and proposed § 1.163(j)–1(b)(1)(i) did not increase the amount of business interest expense the taxpayer could have deducted in the year the deductions were incurred. For example, in 2021, corporation C has \$500x of ATI (computed by adding back \$50x of depreciation deductions with respect to asset X) and \$100x of business interest expense. Without adding back the depreciation deductions, C's ATI would have been \$450x, C's section 163(j) limitation would have been \$135x (\$450x × 30 percent), and C still could have deducted all \$100x of its business interest expense in that year. In 2022, C has \$90x of business interest expense and \$300x of ATI. C sells asset X for a \$50x gain in that year. If C were required to reduce its ATI by \$50x (from \$300x to \$250x) in 2022 under proposed § 1.163(j)–1(b)(1)(ii)(C), its section 163(j) limitation would be reduced to \$75x (\$250x × 30 percent), and C would not be able to deduct all \$90x of its business interest expense in 2022 even though C derived no benefit from adding back its depreciation deductions to taxable income in 2021.

The Treasury Department and the IRS have determined that predicating the application of proposed § 1.163(j)–1(b)(1)(ii)(C), (D), and (E) upon whether a taxpayer derived a benefit under section 163(j) from adding back its depreciation deductions to taxable income would involve significant additional complexity. In addition, this approach would have an effect similar to allowing a carryforward of these amounts to the taxable year in which gain on the related items is recognized on a sale or other disposition. Such a carryforward is inconsistent with the general approach of section 163(j), which does not permit a carryforward of excess ATI to later taxable years. As noted earlier in this part II(A)(5) of this Summary of Comments and Explanation of Revisions section, depreciation deductions should have no net effect on the amount of a taxpayer's taxable income (except with respect to timing and, perhaps, character). Thus, if a taxpayer sells an asset with respect to which the taxpayer has taken depreciation deductions, the increase in gain (or decrease in loss) upon the sale should be reversed under proposed § 1.163(j)–1(b)(1)(ii)(C).

6. Adjustments to Adjusted Taxable Income in Respect of United States Shareholders of CFCs

Some commenters argued that United States shareholders, as defined in section 951(b) (U.S. shareholders), of controlled foreign corporations, as defined in section 957(a) (CFCs), should be allowed to include in their ATI the amounts included in gross income under section 951(a) (subpart F inclusions), section 951A(a) global intangible low-taxed income (GILTI) inclusions, and section 78 ''gross-up'' inclusions (collectively, CFC income inclusions) attributable to non-excepted trades or businesses. Because section 163(j) applies to CFCs, the Treasury Department and the IRS have determined that allowing a U.S. shareholder to include its CFC income inclusions in its ATI would not be appropriate. The income of the CFC that gives rise to such income is taken into account in computing the ATI of the CFC for purposes of determining its section 163(j) limitation, and allowing the same income to also be taken into account in computing the ATI of a U.S. shareholder would result in an inappropriate double-counting of income.

Furthermore, the Treasury Department and the IRS question the premise of several comments that, if the business interest expense of a CFC were excluded from the application of section 163(j), including the income of a CFC in a U.S. shareholder's ATI would be appropriate. Even if section 163(j) did not apply to CFCs, CFCs are entities that also may be leveraged. Thus, permitting the income of the CFC that gives rise to CFC income inclusions attributable to non-excepted trades or businesses of CFCs to be included in the ATI of U.S. shareholders would be inconsistent with the principles of section 163(j).

In particular, consider a case in which a CFC has interest expense of $100x, trade or business gross income of $300x treated as subpart F income, and no foreign tax liability. In such a case, a U.S. shareholder that wholly owns the CFC would have a subpart F inclusion of $200x (if section 163(j) did not apply to CFCs). If the $200x subpart F inclusion were included in the ATI of the U.S. shareholder, the U.S. shareholder could deduct an additional $60x of business interest expense ($200x × 30 percent). As a result, $300x of gross income could support $160x of interest expense deductions rather than the $90x permitted under section 163(j)(1).

Finally, under the final regulations (and consistent with proposed § 1.163(j)–7(d)(1)(ii)), if a domestic partnership includes amounts in gross income under sections 951(a) and 951A(a) with respect to an applicable CFC and such amounts are investment income to the partnership, then, a domestic C corporation partner's distributive share of such amounts that are properly allocable to a non-excepted trade or business of the domestic C corporation by reason of §§ 1.163(j)–4(b)(3) and 1.163(j)–10(c) are excluded from the domestic C corporation partner's ATI.

B. Definition of Business Interest Expense—Proposed § 1.163(j)–1(b)(2)

The proposed regulations provide that business interest expense includes interest expense allocable to a non-excepted trade or business, floor plan financing interest expense, and disallowed business interest expense carryforwards. The Treasury Department and the IRS received informal questions about the interaction between section 163(j) and sections 465 and 469, which may operate to disallow a deduction for business interest expense even if such expense was allowable after the application of section 163(j). More specifically, questions have arisen regarding how to treat amounts of business interest expense that are disallowed under section 465 or 469, including which amounts carry forward to subsequent taxable years but keep their character as interest expense, and which amounts, if any, are business interest expense in such subsequent taxable years.

If amounts of business interest expense that are disallowed under section 465 or 469 are treated as business interest expense in subsequent taxable years, the section 163(j) limitation could operate to disallow a deduction even though such amounts were allowable in the prior taxable year after application of the section 163(j) limitation. The Treasury Department and the IRS do not intend such a result. Therefore, the final regulations clarify that amounts allowable as a deduction after application of the section 163(j) limitation but disallowed by section 465 or 469 are not business interest expense subject to the section 163(j) limitation in subsequent taxable years.

C. Definition of Excepted Regulated Utility Trade or Business—Proposed § 1.163(j)–1(b)(13)

Numerous comments were submitted concerning the definition of an ''excepted regulated utility trade or business'' under proposed § 1.163(j)–1(b)(13). Proposed § 1.163(j)–1(b)(13), which implements the exception in section 163(j)(7)(A)(iv) to the definition of a ''trade or business,'' generally provides that an excepted regulated utility trade or business is a trade or business that sells or furnishes the items listed in section 163(j)(7)(A)(iv) at rates that are established or approved by certain regulatory bodies described in proposed § 1.163(j)–1(b)(13)(i)(B)(*1*) and (*2*).

The proposed regulations provide that utilities that sell or furnish the regulated items at rates that are established or approved by a regulatory body described in proposed § 1.163(j)–1(b)(13)(i)(B)(*1*), other than an electric cooperative, are considered to be excepted only to the extent that such rates are determined on a ''cost of service and rate of return'' basis. The ''cost of service and rate of return'' requirement was intended to provide certainty to taxpayers because many utilities are familiar with the definition of ''cost of service and rate of return,'' which is used to determine whether a public utility company must use a normalization method of accounting under section 168 for certain properties.

However, several commenters questioned whether a ''cost of service and rate of return'' requirement would be satisfied in specific fact patterns. Commenters questioned whether certain negotiated rates are established or approved on a ''cost of service and rate of return'' basis if (1) the applicable regulatory body has the authority to impose a cost-based rate instead of the negotiated rate, (2) the rates are computed with reference to cost but discounted from the recourse (or maximum) rate allowed by the regulatory body, or (3) the rates are computed with reference to cost and a set rate of return but are subject to a market-based cap. Commenters also asked whether the inclusion of certain amounts in determining ''cost of service,'' specifically the costs of affiliates and some revenues attributable to market-rate sales, would affect the determination of whether rates are established or approved on a ''cost of service and rate of return'' basis.

One commenter noted that the normalization rules operate logically only in the ''cost of service and rate of return'' context. The commenter stated that, because section 163(j)(7)(A)(iv) does not reference the normalization rules, there is no need to include the ''cost of service and rate of return'' requirement in the section 163(j) regulations.

The Treasury Department and the IRS note that, in private letter rulings and informal guidance related to section 168(i)(9) and (10), the IRS has stated that, for purposes of applying the normalization rules, the definition of ''public utility property'' must contain the requirement that the regulated rates be established or approved on a ''rate of return'' basis. In this guidance, the IRS explained that the normalization method, which must be used for public utility property to be eligible for the depreciation allowance available under section 168, is defined in terms of the method the taxpayer uses in computing its tax expense in establishing its ''cost of service'' for ratemaking purposes and reflecting operating results in its regulated books of account. Furthermore, the IRS has issued numerous private letter rulings regarding whether under the specific facts of the taxpayer, the cost of service and rate of return requirement has been met for purposes of section 168(i). Thus, it is clear that, in the context of section 168, the ''cost of service and rate of return'' requirement is necessary.

Neither the text of section 163(j) nor the legislative history specifically references the normalization rules or the ''cost of service and rate of return'' requirement under section 168(i)(10). With the omission of such references, the exception in section 163(j) for regulated utility trade or business could be applied broadly without reference to specific requirements applicable in the normalization rules. However, the Treasury Department and the IRS note that under section 168(k)(9), the additional first-year depreciation deduction is not available to any property that is primarily used in an excepted regulated utility trade or business. Therefore, to ease the administrative burden of determining whether businesses qualify as excepted regulated utility trades or businesses, and to allow taxpayers the option of claiming the additional first-year depreciation deduction under section 168(k) in lieu of being treated as an excepted regulated utility trade or business, the final regulations retain the ''cost of service and rate of return'' requirement from the proposed regulations, and also allow taxpayers to make an election to be an excepted regulated utility trade or business to the extent that the rates for the furnishing or sale of the items described in § 1.163(j)–1(b)(15)(i)(A)(*1*) have been established or approved by a regulatory body described in § 1.163(j)–1(b)(15)(i)(A)(*2*), if the rates are not determined on a ''cost of service and rate of return'' basis. See § 1.163(j)–1(b)(15)(i) and (iii).

For purposes of the election, the focus of section 163(j)(7)(A)(iv) is the phrase ''established or approved'' in section 163(j)(7)(A)(iv), which describes the authority of the regulatory body described in § 1.163(j)–1(b)(15)(i)(A)(*2*). Ratemaking programs similar to those described by commenters and discussed previously in this part II(C) of this Summary of Comments and Explanation of Revisions section, including discounted rates, negotiated rates, and regulatory rate caps, are established or approved by a regulatory body if the taxpayer files a schedule of such rates with a regulatory body that has the power to approve, disapprove, alter the rates, or substitute a rate determined in an alternate manner.

Similar to elections for electing real property trades or businesses and electing farming businesses, the election to be an excepted regulated utility trade or business is irrevocable. Taxpayers making the election to be an excepted regulated utility trade or business are not required to allocate items between regulated utility trades or businesses that are described in § 1.163(j)–1(b)(15)(i) and trades or businesses that are described in § 1.163(j)–1(b)(15)(iii)(A) as to which the taxpayer makes an election because they are treated as operating an entirely excepted regulated utility trade or business. Electing taxpayers cannot claim the additional first-year depreciation deduction under section 168(k).

The rules set forth in the final regulations are limited solely to the determination of an ''excepted regulated utility trade or business'' for purposes of section 163(j)(7)(A)(iv). As a result of this limited application, the rules in the final regulations are not applicable to the determination of ''public utility property'' or the application of the normalization rules within the meaning of section 46(f), as in effect on the day before the date of the enactment of the Revenue Reconciliation Act of 1990, section 168(i)(9) and (10) and the regulations thereunder, or to the determination of any depreciation allowance available under sections 167 and 168.

Comments also were received on the application of the rules for excepted regulated utility trades or businesses to electric cooperatives. The definition of an ''excepted regulated utility trade or business'' under proposed § 1.163(j)–1(b)(13) includes trades or businesses that sell or furnish the items listed in section 163(j)(7)(A)(iv) at rates established or approved by an electric cooperative. Unlike utility businesses regulated by public authorities, utilities that sell items at rates regulated by a cooperative are not described in section 168(i)(10). However, there is a long-standing body of law regulating the taxation of electric cooperatives. Electric cooperatives described in section 501(c)(12) are generally exempt from income tax but are subject to taxation under section 511. The application of section 163(j) and the section 163(j) regulations with respect to exempt electric cooperatives is governed by proposed § 1.163(j)–4(b)(5). Other electric cooperatives are subject to taxation under sections 1381 through 1388 in subchapter T of chapter 1 of subtitle A of the Code (subchapter T), except for certain rural electric cooperatives specifically excluded from subchapter T by section 1381(a)(2)(C).

Generally, the exception in section 163(j)(7)(A)(iv) for the trade or business of selling or furnishing items at rates established or approved by the governing or ratemaking body of an electric cooperative applies both to sales and furnishing by an electric cooperative and to sales and furnishing to an electric cooperative by another utility provider, as long as the rates for the sale or furnishing have been established or approved in the manner required by section 163(j). Thus, an electric cooperative exempt from Federal income tax under section 501(c)(12) may not be subject to section 163(j) for the sale or furnishing of electricity due to the operation of proposed § 1.163(j)–4(b)(5), and another utility provider may be in an excepted regulated utility trade or business to the extent that it sells electricity to the section 501(c)(12) cooperative at rates established or approved by the governing or ratemaking body of the cooperative.

A commenter asked whether proposed § 1.163(j)–1(b)(13) requires that, for sales involving electric cooperatives to qualify as an excepted regulated utility trade or business, the rates for the sales be established or approved by the governing or ratemaking body of an electric cooperative on a ''cost of service and rate of return'' basis, or if all sales made subject to a contract or tariff approved by an electric cooperative's governing or ratemaking body would qualify. Under the proposed regulations, the specific requirement that rates for the sale or furnishing of items listed in proposed § 1.163(j)–1(b)(13)(i)(A) be established or approved on a ''cost of service and rate of return'' basis did not extend to rates established or approved by the governing or ratemaking body of an electric cooperative. These regulations adopt the proposed rule, and do not impose a requirement that rates for the sale or furnishing of items listed in § 1.163(j)–1(b)(15)(i)(A) by an electric cooperative be established or approved on a ''cost of service and rate of return'' basis.

Comments also were submitted regarding the allocation of tax items between excepted regulated utility trades or businesses and non-excepted trades or businesses. These comments are discussed with other comments on proposed § 1.163(j)–10 in part XI of this Summary of Comments and Explanation of Revisions section.

D. Definition of Floor Plan Financing Interest Expense—Proposed § 1.163(j)–1(b)(17)

Commenters recommended that interest paid on commercial financing liabilities or trade financing (in which a taxpayer borrows to fund the purchase or transport of commodities and then sells the inventory to pay off the debt) should not be subject to section 163(j). Commenters noted that trade financing is different from normal financing because it is short-term and backed by inventory that is monetizable (rather than plant and equipment). Thus, commenters suggested that section 163(j) should not apply to trade financing because there is no depreciation trade-off for inventory purchased with trade financing. Commenters compared trade financing to floor plan financing (because both are used to finance the purchase of inventory), and they noted that the 1991 Proposed Regulations under old section 163(j) excluded commercial financing liabilities from debt taken into account for purposes of applying the debt-equity ratio under old section 163(j). See 1991 Proposed Regulations § 1.163(j)–3(b)(2)(ii).

The Treasury Department and the IRS decline to exclude commercial financing liabilities from the section 163(j) limitation. Section 163(j) does not contain a provision analogous to the debt-equity ratio safe harbor that was present in old section 163(j) and for which rules were proposed in the 1991 Proposed Regulations. In addition, because Congress specifically excluded interest paid on floor plan financing from the section 163(j) limitation, but not all commercial financing liabilities and trade financing, Congress does not appear to have intended to exclude all commercial financing liabilities from the section 163(j) limitation.

E. Definition of Interest—Proposed § 1.163(j)–1(b)(20)

1. In General

Commenters submitted numerous comments on the definition of ''interest'' in the proposed regulations. Proposed § 1.163(j)–1(b)(20) contains a relatively broad definition of the term ''interest'' for purposes of section 163(j). This definition was proposed to provide a complete definition of interest that addresses all transactions that are commonly understood to produce interest income and expense, including transactions that otherwise may have been entered into to avoid the application of section 163(j).

Under the proposed regulations, the term ''interest'' means any amount described in one of four categories. First, proposed § 1.163(j)–1(b)(20)(i) generally provides that interest is an amount paid, received, or accrued as compensation for the use or forbearance of money under the terms of an instrument or contractual arrangement, including a series of transactions, that is treated as a debt instrument, or an amount that is treated as interest under other provisions of the Code or the Income Tax Regulations. For example, this category includes qualified stated interest, original issue discount (OID), and accrued market discount. Commenters agree that this definition of interest has long been accepted, is consistent with longstanding precedent, and reduces the risk of inconsistency within the Code and regulations. No commenters requested any changes to this category, and the final regulations adopt this category in the definition of the term ''interest'' without any substantive changes.

Second, proposed § 1.163(j)–1(b)(20)(ii) treats a swap (other than a cleared swap) with significant nonperiodic payments as two separate transactions consisting of an on-market, level payment swap and a loan. Under the proposed regulations, the time value component of the loan is recognized as interest expense to the payor and as interest income to the recipient. Several comments were received on this category in the definition and are described in part II(E)(2) of this Summary of Comments and Explanation of Revisions section.

Third, proposed § 1.163(j)–1(b)(20)(iii) treats as interest certain amounts that are closely related to interest and that affect the economic yield or cost of funds of a transaction involving interest, but that may not be compensation for the use or forbearance of money on a stand-alone basis. For example, this category includes substitute interest payments, debt issuance costs, commitment fees, and hedging gains and losses that affect the yield of a debt instrument. Numerous comments were received on this category and are described in part II(E)(3) of this Summary of Comments and Explanation of Revisions section.

Fourth, proposed § 1.163(j)–1(b)(20)(iv) provides an anti-avoidance rule. Under this rule, an expense or loss predominantly incurred in consideration of the time value of money in a transaction or series of integrated or related transactions in which a taxpayer secures the use of funds for a period of time is treated as interest expense for purposes of section 163(j). Numerous comments were received on this category and are described in part II(E)(4) of this Summary of Comments and Explanation of Revisions section.

2. Swaps With Significant Nonperiodic Payments

The proposed regulations treat a non-cleared swap with significant nonperiodic payments as two separate transactions consisting of an on-market, level payment swap and a loan (the embedded loan rule). The embedded loan rule did not apply to a collateralized swap that was cleared by a derivatives clearing organization or by a clearing agency (a cleared swap) because the treatment of cleared swaps was reserved. In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments on the proper treatment of collateralized swaps under the embedded loan rule.

One commenter recommended that the final regulations provide an exception to the embedded loan rule for cleared swaps and for non-cleared swaps that are substantially collateralized. This commenter further suggested that the final regulations not include any specific rules regarding the type of collateral that is required to be posted to qualify for the exception. The commenter also recommended that the final regulations provide objective rules for determining if a nonperiodic payment is ''significant'' and if a financial instrument is treated as a ''swap'' for purposes of these rules.

Another commenter agreed with the embedded loan rule, including use of the ''significant'' standard, and also recommended exceptions to the embedded loan rule for both cleared swaps and non-cleared swaps that are required to be fully collateralized by the terms of the swap contract or by a federal regulator. However, this commenter interpreted the embedded loan rule in the proposed regulations to apply solely for purposes of section 163(j) and recommended that the embedded loan rule, as well as timing and character rules for nonperiodic payments on swaps, be issued under section 446. Until that guidance is issued, the commenter requested that the application of the embedded loan rule for purposes of section 163(j) be delayed. The proposed regulations provide that the time value component of the embedded loan is determined in accordance with § 1.446–3(f)(2)(iii)(A). This commenter questioned the reference to § 1.446–3(f)(2)(iii)(A) because, under that rule, the time value component is not treated as interest; rather, the time value component is only used to compute the amortization of the nonperiodic payment.

As a result of the cross-reference in proposed § 1.446–3(g)(4) to proposed § 1.163(j)–1(b)(20)(ii), the embedded loan rule set forth in the proposed regulations applies for purposes of both sections 163(j) and 446. In addition, and as noted in the preamble to the proposed regulations, the embedded loan rule set forth in the proposed regulations applies in the same manner that former § 1.446–3(g)(4) applied before it was amended by the now expired temporary regulations in T.D. 9719 (80 FR 26437) (May 8, 2015) (as corrected by 80 FR 61308 (October 13, 2015)). The Treasury Department and the IRS do not adopt commenters' suggestions to delay finalizing the embedded loan rule or to provide guidance on determining if a nonperiodic payment is ''significant'' because the same embedded loan rule applied in the context of section 446 for over 20 years from 1993 to 2015. See T.D. 8491 (58 FR 53125) (October 14, 1993). Instead, subject to the exceptions discussed in this part II(E)(2) of this Summary of Comments and Explanation of Revisions section, the final regulations adopt the embedded loan rule without change. The final regulations retain the reference to § 1.446–3(f)(2)(iii)(A), which provides a known method for computing the time value component associated with the loan component that is treated as interest under §§ 1.163(j)–1(b)(22)(ii) and 1.446–3(g)(4).

Further, to eliminate the possibility of confusion regarding the application of the embedded loan rule for purposes of sections 163(j) and 446, the final regulations add the substantive text of the embedded loan rule and the exceptions to that rule to both §§ 1.446–3(g)(4) and 1.163(j)–1(b)(22)(ii) instead of merely including a cross-reference in § 1.446–3(g)(4) to § 1.163(j)–1(b)(22)(ii).

In response to comments, the final regulations add two exceptions to the embedded loan rule. Specifically, the final regulations add exceptions for cleared swaps and for non-cleared swaps that require the parties to meet the margin or collateral requirements of a federal regulator or that provide for margin or collateral requirements that are substantially similar to a cleared swap or a non-cleared swap subject to the margin or collateral requirements of a federal regulator. For purposes of this exception, the term ''federal regulator'' means the Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), or a prudential regulator, as defined in section 1a(39) of the Commodity Exchange Act (7 U.S.C. 1a), as amended by section 721 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Public Law 111–203, 124 Stat. 1376, Title VII (the Dodd-Frank Act). Because federal regulators have adopted final requirements for non-cleared swaps that permit netting of swap exposures and specify the types of collateral required to be posted, the final regulations do not address netting or require that the margin or collateral be paid or received in cash.

In addition, § 1.163(j)–1(c)(3)(i) delays the applicability date of the embedded loan rule for purposes of section 163(j) to allow taxpayers additional time to develop systems to implement these rules (the delayed applicability date), though taxpayers may choose to apply the rules to swaps entered into before the delayed applicability date. See also § 1.446–3(j)(2), which provides applicability date rules similar to those in § 1.163(j)–1(c)(3)(i). However, the delayed applicability date does not apply for purposes of the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) (described in part II(E)(4) of this Summary of Comments and Explanation of Revisions section). Instead, the applicability date in § 1.163(j)–1(c)(3)(ii) applies. As a result, the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) apply to a notional principal contract entered into on or after September 14, 2020. However, for a notional principal contract entered into before September 14, 2021, the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) apply without regard to the references in those rules to § 1.163(j)–1(b)(22)(ii). For example, if a taxpayer enters into a swap with a significant nonperiodic payment that does not meet the exceptions in § 1.163(j)–1(b)(22)(ii)(B) or (C) before the delayed applicability date, and a principal purpose of the taxpayer is to reduce the amount that otherwise would be interest expense, the anti-avoidance rules apply and the taxpayer must treat the time value component associated with the loan component of the swap as interest expense.

3. Other Amounts Treated as Interest

i. Items Relating to Premium, Ordinary Income or Loss on Certain Debt Instruments, Section 1258 Gain, and Factoring Income

Proposed § 1.163(j)–1(b)(20)(iii)(A) treats any bond issuance premium treated as ordinary income under § 1.163–13(d)(4) as interest income of the issuer and any amount deductible as a bond premium deduction under § 1.171–2(a)(4)(i)(A) or (C) as interest expense of the holder. Proposed § 1.163(j)–1(b)(20)(iii)(B) treats any ordinary income recognized by an issuer of a debt instrument, and any ordinary loss recognized by a holder of a debt instrument, under the rules for a contingent payment debt instrument, a nonfunctional currency contingent payment debt instrument, or an inflation-indexed debt instrument, as interest income of the issuer and as interest expense of the holder, respectively. Proposed § 1.163(j)–1(b)(20)(iii)(D) treats any ordinary gain under section 1258 as interest income. Commenters supported treating the amounts in proposed § 1.163(j)–1(b)(20)(iii)(A), (B), and (D) as interest income or interest expense for purposes of section 163(j). Accordingly, the final regulations adopt the rules in the proposed regulations for these three items without any substantive changes.

Proposed § 1.163(j)–1(b)(20)(iii)(J) treats factoring income as interest income. Several commenters supported treating factoring income as interest income. However, one commenter questioned the differences between the provisions related to the inclusion of factoring income and § 1.954–2(h)(4). The inclusion of factoring income in the definition of interest is generally supported by the commenters, is a taxpayer-favorable rule, is generally consistent with the rules in § 1.954–2(h)(4), and is consistent with the treatment of other types of discount, such as acquisition discount and market discount. Accordingly, the final regulations adopt the rules in the proposed regulations for factoring income without any substantive changes. In the case of a factoring transaction with a principal purpose of artificially increasing a taxpayer's business interest income, the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) (described in part II(E)(4) of this Summary of Comments and Explanation of Revisions section) would not permit the taxpayer to treat factoring income as interest income for purposes of section 163(j).

ii. Substitute Interest Payments

Proposed § 1.163(j)–1(b)(20)(iii)(C) generally provides that a substitute interest payment described in § 1.861–2(a)(7) and made in connection with a sale-repurchase or securities lending transaction is treated as interest expense to the payor and interest income to the recipient. In general, substitute interest payments are economically equivalent to interest. A few commenters questioned the inclusion of substitute interest payments in the definition of interest in the proposed regulations. Commenters stated that treating these amounts as interest would be contrary to longstanding tax law, including the holding in *Deputy* v. *Du Pont,* 308 U.S. 488, 498 (1940). However, commenters recommended that, if the Treasury Department and the IRS decide to include substitute interest payments in the definition of interest in the final regulations, the inclusion be limited to the extent the substitute interest payments relate to transactions that are economically similar to a borrowing. Commenters recommended that the following factors be taken into consideration in making this determination: (a) Whether the taxpayer posted (or has received) collateral consisting of cash or liquid assets; (b) whether the borrowed security is due to mature shortly after the scheduled termination date of the securities borrowing; (c) the type of security being lent (for example, Treasury bonds as compared to riskier corporate bonds); and (d) whether the securities borrowing was entered into in the ordinary course of the taxpayer's trade or business.

The final regulations retain substitute interest payments in the definition of interest because the payments generally are economically equivalent to interest and should be treated as such for purposes of section 163(j). However, in response to comments, the final regulations provide that a substitute interest payment is treated as interest expense to the payor only if the payment relates to a sale-repurchase or securities lending transaction that is not entered into by the payor in the payor's ordinary course of business, and that a substitute interest payment is treated as interest income to the recipient only if the payment relates to a sale-repurchase or securities lending transaction that is not entered into by the recipient in the recipient's ordinary course of business. The final regulations do not adopt the other suggested factors because the Treasury Department and the IRS have determined that the ordinary course rule in the final regulations provides an appropriate and effective limit on the scope of the definition. Specifically, the Treasury Department and the IRS have determined that these transactions are rarely entered into outside the payor's ordinary course of business, and that any such non-ordinary course transactions likely would involve an intention to avoid section 163(j).

iii. Commitment Fees

Proposed § 1.163(j)–1(b)(20)(iii)(G)(*1*) treats any fees in respect of a lender commitment to provide financing as interest if any portion of such financing is actually provided. Commenters recommended that commitment fees and other debt-related fees not be included in the definition of interest until general substantive guidance is provided on the treatment of the fees in the separate fee-related project on the Office of Tax Policy and IRS 2019–2020 Priority Guidance Plan (REG–132517–17). According to the commenters, uncertainty exists as to whether to characterize these fees for Federal income tax purposes as fees for services or property or for compensation for the use or forbearance of money. In addition, under existing guidance, commitment fees are treated differently by the borrower (similar to an option premium) and the lender (service income). See Rev. Rul. 81–160, 1981–1 C.B. 312, and Rev. Rul. 70–540, 1970–2 C.B. 101, Situation (3). Some taxpayers, however, argue that a commitment fee should be treated as creating or increasing discount on a debt instrument and that the fee should be treated consistently by both the borrower and the lender. If commitment fees are included in the definition of interest in the final regulations, commenters recommended that only the portion of the commitment fee that is proportionate to the amount drawn be treated as interest.

In response to comments, the final regulations do not include commitment fees in the definition of interest. The treatment of commitment fees and other fees paid in connection with lending transactions will be addressed in future guidance that applies for all purposes of the Code.

iv. Debt Issuance Costs

Proposed § 1.163(j)–1(b)(20)(iii)(H) treats debt issuance costs as interest expense of the issuer. Commenters argued that debt issuance costs should not be treated as interest expense because these costs are paid to third parties in connection with the issuance of debt and are not paid or incurred for the use or forbearance of money under a debt instrument. For tax purposes, these costs are capitalized by the issuer and are treated as deductible under section 162 over the term of the debt instrument as if the costs adjust the instrument's yield by reducing the instrument's issue price by the amount of the costs. See § 1.446–5.

In response to comments, the final regulations exclude debt issuance costs from the definition of interest.

v. Guaranteed Payments

Proposed § 1.163(j)–1(b)(20)(iii)(I) provides that any guaranteed payments for the use of capital under section 707(c) are treated as interest. Some commenters stated that a guaranteed payment for the use of capital should not be treated as interest for purposes of section 163(j) unless the guaranteed payment was structured with a principal purpose of circumventing section 163(j). Other commenters stated that section 163(j) never should apply to guaranteed payments for the use of capital.

In response to comments, the final regulations do not explicitly include guaranteed payments for the use of capital under section 707(c) in the definition of interest. However, consistent with the recommendations of some commenters, the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) (described in part II(E)(4) of this Summary of Comments and Explanation of Revisions section) include an example of a situation in which a guaranteed payment for the use of capital is treated as interest expense and interest income for purposes of section 163(j). See § 1.163(j)–1(b)(22)(v)(E), *Example 5.*

vi. Hedging Transactions

Proposed § 1.163(j)–1(b)(20)(iii)(E) generally treats income, deduction, gain, or loss from a derivative that alters a taxpayer's effective cost of borrowing with respect to a liability of the taxpayer as an adjustment to the taxpayer's interest expense. Proposed § 1.163(j)–1(b)(20)(iii)(F) generally treats income, deduction, gain, or loss from a derivative that alters a taxpayer's effective yield with respect to a debt instrument held by the taxpayer as an adjustment to the taxpayer's interest income. The rules in the two provisions are referred to as the ''hedging rules'' in this preamble.

Numerous comments were received on the hedging rules. The commenters questioned the administrability of the broad hedging rules, especially if the taxpayer hedges on a macro (that is, on an aggregate) basis. Also, the commenters noted that it is not clear how to apply the rules in certain situations, including a situation in which the hedge relates to non-debt items (for example, if the taxpayer hedges the mismatch or ''gap'' between its assets and liabilities), the debt instrument is not subject to section 163(j), or the debt instrument is subject to other interest deferral provisions for Federal tax purposes. In addition, the commenters noted that the proposed regulations effectively would require integration, even if the hedge otherwise would not be integrated with the debt instrument for Federal tax purposes and the income, deduction, gain, and loss from the hedge ordinarily would be accounted for separately, which the commenters suggested would require taxpayers to maintain two sets of books. Moreover, the commenters stated that, under the proposed regulations, any gain or loss on the underlying debt instrument (for example, due to changes in interest rates) would not be treated as an adjustment to interest income or expense, whereas the corresponding loss or gain on the hedge would be treated as an adjustment to interest expense or income. Some commenters stated that the yield on third-party borrowings reflects the true cost of the borrowing, and that hedges are not relevant to the cost of the borrowing.

Commenters recommended that, if the hedging rules are retained in the final regulations as a separate item, the final regulations precisely define (a) what standard is used to include a derivative in section 163(j) (for example, a primary purpose or principal motivation standard), and (b) the standard for determining whether the effect of a derivative on the cost of borrowing or effective yield is sufficiently significant for the income, deduction, gain, or loss from the derivative to be included in the computation. Commenters noted that one approach would be to apply the hedging rules only to derivatives that qualify for integration under § 1.988–5 or § 1.1275–6. Another approach would be to apply the hedging rules to derivatives that have a sufficiently close connection with the liability to qualify as hedging transactions under §§ 1.446–4 and 1.1221–2. Some commenters indicated that the hedging rules could apply if the derivative is treated as a hedge of a borrowing or liability for financial reporting purposes, and that the hedging rules should not apply to broker-dealers, active traders in derivatives, and financial institutions acting in the ordinary course of business.

One commenter recommended that section 163(j) not alter the timing of taxable items from hedging transactions that are subject to § 1.446–4, regardless of whether interest expense on the hedged item is deferred under section 163(j). Other commenters noted that the proposed regulations do not provide guidance on the interaction between the hedging rules and the straddle rules.

With respect to foreign currency hedging transactions, a commenter noted that foreign currency gain or loss is due to the time value of money only to a limited extent; thus, the commenter recommended that section 163(j) not apply to a taxpayer's foreign currency hedging transactions (other than an integrable transaction under § 1.988–5).

In response to comments, the final regulations do not include the hedging rules in the definition of interest. However, in certain circumstances, the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) (described in part II(E)(4) of this Summary of Comments and Explanation of Revisions section) may apply to require income, deduction, gain, or loss from a hedging transaction to be taken into account for purposes of section 163(j).

vii. Other Items

Commenters recommended other items to be included in, or excluded from, the definition of interest as follows:

a. Dividends From Regulated Investment Company (RIC) Shares

Some commenters recommended that dividend income from a RIC be treated as interest income for a shareholder in a RIC, to the extent that the dividend is attributable to interest income earned by the RIC. To address this comment, in the Concurrent NPRM, the Treasury Department and the IRS have proposed rules under which a RIC that earns business interest income may pay section 163(j) interest dividends that certain shareholders may treat as interest income for purposes of section 163(j). See paragraphs (b)(22)(iii)(F) and (b)(35) in proposed § 1.163(j)–1 in the Concurrent NPRM.

b. MMF Income

A few commenters recommended that the final regulations allow look-through treatment for earnings from certain foreign entities, such as foreign money market funds (MMFs), so that dividends from foreign MMFs would be treated as interest income to the extent the underlying income derived by a foreign MMF was interest income. According to the commenters, this treatment would alleviate issues for a CFC that borrows money from related parties and invests in foreign MMFs. In general, the commenters stated that any interest limitation under section 163(j) could lead to unexpected results in this situation, such as section 952(c) recapture accounts solely generated by the section 163(j) interest expense limitation.

The final regulations do not adopt this recommendation because it is beyond the scope of the final regulations and because there are significant differences between the rules governing income inclusions in respect of passive foreign investment companies (PFICs), such as foreign MMFs, and RICs. These differences make it difficult to adopt a rule that would provide for look-through treatment in the context of dividends or inclusions from a PFIC. In particular, the regime for taxing income from a PFIC that shareholders have elected to treat as a qualified electing fund (QEF) under section 1295 generally focuses only on inclusions related to ordinary income or net capital gain income and does not separately report amounts of interest income for Federal income tax purposes. In the case of a PFIC for which a QEF election has not been made, there would be no information about the underlying taxable income of the PFIC and no reason or ability to treat an interest in the PFIC differently from the treatment of stock held in other C corporations.

c. Negative Interest

One commenter requested clarification on the treatment of negative interest (an amount that a depositor may owe a bank in a negative interest rate environment) and inquired whether such payments are more similar to payments for custodial or service fees rather than for interest. The final regulations do not address this issue because it is beyond the scope of the final regulations. However, in certain cases (for example, a Treasury bill acquired with a negative yield), a payment may be treated as bond premium subject to the rules in section 171, including the rules in § 1.171–2(a)(4)(i)(C).

d. Leases

A commenter recommended that the Treasury Department and the IRS adopt rules that clearly describe the circumstances in which fleet leases are treated as generating interest for purposes of section 163(j). The commenter noted that there is a time-value-of-money portion of a fleet lease payment similar to the time-value-of-money portion of other items treated as interest under the proposed regulations, such as guaranteed payments, commitment fees, debt issuance costs, and items of income or loss from a derivative instrument that alters a taxpayer's effective yield or effective cost of borrowing. In addition, to the extent that the anti-avoidance rule in the proposed regulations is retained, the commenter asked that the final regulations clearly define the circumstances (if any) in which the anti-avoidance rule would operate to recharacterize any portion of a fleet lease payment as interest expense, and modify the anti-avoidance rule to apply to both interest expense of the fleet lessee and interest income of the fleet lessor.

The Treasury Department and the IRS do not adopt the commenter's suggestions in the final regulations because the suggestions generally are no longer relevant after the revisions made to the definition of interest in the final regulations. For example, as explained in this part II(E)(3) of this Summary of Comments and Explanation of Revisions section, no portion of the items generally cited by the commenter is explicitly treated as interest in the final regulations. Moreover, there are explicit provisions in the Code that determine whether a portion of a lease payment is treated as interest for Federal income tax purposes depending on the terms of a lease, such as sections 467 and 483. In addition, as explained in part II(E)(4) of this Summary of Comments and Explanation of Revisions section, the anti-avoidance rule in the final regulations is revised to include a principal purpose test and to generally align the treatment of income and expense, which should address the commenter's concerns.

4. Anti-Avoidance Rule for Amounts Predominantly Associated With the Time Value of Money

Proposed § 1.163(j)–1(b)(20)(iv) provides that any expense or loss, to the extent deductible, incurred by a taxpayer in a transaction or series of integrated or related transactions in which the taxpayer secures the use of funds for a period of time is treated as interest expense of the taxpayer if such expense or loss is predominantly incurred in consideration of the time value of money. Numerous comments were received on this anti-avoidance rule in the proposed regulations. Most commenters recommended that any anti-avoidance rule in the final regulations contain a requirement that the taxpayer have a principal purpose to avoid section 163(j). Several commenters asserted that the anti-avoidance rule should cover only transactions that are economically equivalent to interest and should set forth examples of transactions that are and are not covered. Most commenters recommended that the anti-avoidance rule be symmetrical and apply to income or gain, as well as to expense or loss. One commenter suggested that, based on section 1258 concepts, the anti-avoidance rule should apply only if, at the time of the relevant transaction or series of transactions that secure the use of funds for a period of time for the taxpayer, substantially all of the expense or loss was expected to be attributable to the time value of money. In addition, commenters noted that it should be clear when a taxpayer should test whether a transaction falls within the anti-avoidance rule. Other commenters requested specific rules coordinating this anti-avoidance rule with the general anti-avoidance rule in proposed § 1.163(j)–2(h).

Some commenters stated that an interest anti-avoidance rule should not be included in the final regulations because, for example, the rule would impose substantial compliance costs, the Treasury Department and the IRS have other tools to combat any abuse, and there already is a general anti-avoidance rule in proposed § 1.163(j)–2(h). Commenters also noted that the interest anti-avoidance rule in the proposed regulations has the potential to capture ordinary market transactions that possess a time value component but that are not generally treated as financings with disguised interest for tax purposes.

In response to comments, the Treasury Department and the IRS have modified the anti-avoidance rule in the final regulations. Under § 1.163(j)–1(b)(22)(iv)(A)(*1*), any expense or loss economically equivalent to interest is treated as interest expense for purposes of section 163(j) if a principal purpose of structuring the transaction(s) is to reduce an amount incurred by the taxpayer that otherwise would have been interest expense or treated as interest expense under § 1.163(j)–1(b)(22)(i) through (iii). For this purpose, the fact that the taxpayer has a business purpose for obtaining the use of funds does not affect the determination of whether the manner in which the taxpayer structures the transaction(s) is with a principal purpose of reducing the taxpayer's interest expense. In addition, the fact that the taxpayer has obtained funds at a lower pre-tax cost based on the structure of the transaction(s) does not affect the determination of whether the manner in which the taxpayer structures the transaction(s) is with a principal purpose of reducing the taxpayer's interest expense.

For purposes of § 1.163(j)–1(b)(22)(iv)(A)(*1*), any expense or loss is economically equivalent to interest to the extent that the expense or loss is (1) deductible by the taxpayer; (2) incurred by the taxpayer in a transaction or series of integrated or related transactions in which the taxpayer secures the use of funds for a period of time; (3) substantially incurred in consideration of the time value of money; and (4) not described in § 1.163(j)–1(b)(22)(i), (ii), or (iii).

Under § 1.163(j)–1(b)(22)(iv)(A)(*2*), if a taxpayer knows that an expense or loss is treated by the payor as interest expense under § 1.163(j)–1(b)(22)(iv)(A)(*1*), the taxpayer provides the use of funds for a period of time in the transaction(s) subject to § 1.163(j)–1(b)(22)(iv)(A)(*1*), the taxpayer earns income or gain with respect to the transaction(s), and such income or gain is substantially earned in consideration of the time value of money provided by the taxpayer, such income or gain is treated as interest income for purposes of section 163(j) to the extent of the expense or loss treated by the payor as interest expense under § 1.163(j)–1(b)(22)(iv)(A)(*1*).

Under § 1.163(j)–1(b)(22)(iv)(B), notwithstanding § 1.163(j)–1(b)(22)(i) through (iii), any income realized by a taxpayer in a transaction or series of integrated or related transactions is not treated as interest income of the taxpayer for purposes of section 163(j) if and to the extent that a principal purpose for structuring the transaction(s) is to artificially increase the taxpayer's business interest income. For this purpose, the fact that the taxpayer has a business purpose for holding interest-generating assets does not affect the determination of whether the manner in which the taxpayer structures the transaction(s) is with a principal purpose of artificially increasing the taxpayer's business interest income.

For purposes of the foregoing anti-avoidance rules, § 1.163(j)–1(b)(22)(iv)(C) provides that whether a transaction or a series of integrated or related transactions is entered into with a principal purpose depends on all the facts and circumstances related to the transaction(s), except that the fact that the taxpayer has obtained funds at a lower pre-tax cost based on the structure of the transaction(s) or the fact that the taxpayer has a business purpose related to the item is ignored for this purpose. A purpose may be a principal purpose even though it is outweighed by other purposes taken together or separately. Factors to be taken into account in determining whether one of the taxpayer's principal purposes for entering into the transaction(s) include the taxpayer's normal borrowing rate in the taxpayer's functional currency, whether the taxpayer would enter into the transaction(s) in the ordinary course of the taxpayer's trade or business, whether the parties to the transaction(s) are related persons (within the meaning of section 267(b) or section 707(b)), whether there is a significant and bona fide business purpose for the structure of the transaction(s), whether the transactions are transitory, for example, due to a circular flow of cash or other property, and the substance of the transaction(s).

In response to comments, § 1.163(j)–1(b)(22)(iv)(D) provides that the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv), rather than the general anti-avoidance rules in § 1.163(j)–2(j), apply to determine whether an item is treated as interest expense or interest income.

Section 1.163(j)–1(b)(22)(v) contains examples illustrating the application of the interest anti-avoidance rules in a number of situations, including examples relating to a hedging transaction involving a foreign currency swap transaction, a forward contract involving gold, a loan guaranteed by a related party in which the related party receives guarantee fees, and guaranteed payments for the use of capital. However, these examples are not intended to represent the only situations in which the anti-avoidance rules might apply.

The anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) apply to transactions entered into on or after September 14, 2020. See § 1.163(j)–1(c)(2).

5. Authority Comments

Most of the commenters on the definition of interest in the proposed regulations questioned whether the Treasury Department and the IRS have the authority to expand the definition of interest for purposes of section 163(j) to include ''interest equivalents'' (the items listed in proposed § 1.163(j)–1(b)(20)(iii) and the expenses or losses subject to the anti-avoidance rule in proposed § 1.163(j)–1(b)(20)(iv)). The commenters asserted that the term ''business interest'' in section 163(j)(5) means any interest paid or accrued on indebtedness properly allocable to a trade or business, and that expanding the definition to include interest equivalents would capture amounts that do not fall within the scope of the general rule in section 163(a) that ''[t]here shall be allowed as a deduction all interest paid or accrued within the taxable year on indebtedness.'' Even though section 163(j)(1) refers to an ''amount allowed as a deduction under this chapter for business interest'' when describing the amounts limited by section 163(j), the commenters argued that the deduction otherwise allowed must be with respect to ''business interest'' (which is defined in section 163(j)(5)) and that the phrase ''deduction under this chapter'' does not and should not modify the definition of ''business interest'' in section 163(j)(5).

The commenters noted that section 163(j), as amended by the TCJA, does not contain a specific delegation of regulatory authority to expand the definition of interest. The commenters further asserted that the Treasury Department and the IRS may issue only ''interpretive regulations'' under section 7805, and that any such regulations may not go beyond the stated meaning of the statutory language. The commenters noted that old section 163(j)(9) provided broad regulatory authority to prescribe regulations, including regulations appropriate to prevent the avoidance of old section 163(j). In addition, the commenters noted that the legislative history for old section 163(j) indicated that the Treasury Department could issue guidance treating ''items not denominated as interest but appropriately characterized as equivalent to interest'' as interest income or interest expense. The commenters stated that there is no similar regulatory authority or legislative history relating to section 163(j) as amended by the TCJA.

Commenters also noted that, when Congress has chosen to expand the definition of interest in other parts of the Code, Congress has done so explicitly. For example, section 263(g) provides that, ''[for purposes of section 263(g)(2)(A)], the term 'interest' includes any amount paid or incurred in connection with personal property used in a short sale.'' As noted in the preamble to the proposed regulations, most of the rules treating interest equivalent items as interest income or expense in proposed § 1.163(j)–1(b)(20)(iii) were developed in §§ 1.861–9T and 1.954–2. However, commenters argued that the use of the interest equivalent provisions in §§ 1.861–9T and 1.954–2 by analogy to define interest for purposes of section 163(j) is inappropriate because different policy considerations underlie those sections, there is statutory or regulatory authority to address interest equivalents under those sections (unlike section 163(j)), and those sections apply only for limited purposes (for example, for sourcing purposes).

In addition, because the broad definition of interest in the proposed regulations applies only for purposes of section 163(j), commenters asserted that there will be additional compliance burdens and costs for taxpayers to separately track amounts treated as interest for purposes of section 163(j) and for other purposes. Commenters asserted that the broad definition of interest for purposes of section 163(j) in the proposed regulations may create uncertainty and confusion for taxpayers with respect to other sections of the Code.

Contrary to the assertions made by many of the commenters, the Treasury Department and the IRS have the authority to prescribe rules relating to interest equivalents and an anti-avoidance rule. As noted in the preamble to the proposed regulations, there are no generally applicable regulations or statutory provisions addressing when financial instruments are treated as indebtedness for Federal income tax purposes or when a payment is ''interest.'' Therefore, a regulatory definition of interest is needed in order to implement the statutory language of section 163(j).

In addition, it would be inconsistent with the purpose of section 163(j) to allow transactions that are essentially financing transactions to avoid the application of section 163(j). Thus, an anti-avoidance rule is needed to address situations in which a taxpayer's principal purpose in structuring a transaction or series of transactions is to artificially reduce the taxpayer's business interest expense or to increase the taxpayer's business interest income. Moreover, at least one commenter suggested the inclusion of the type of anti-avoidance rule that is included in the final regulations and that the Treasury Department and the IRS have the authority to include such a rule.

Section 7805(a) provides the Treasury Department and the IRS with the authority to prescribe all rules and regulations needed for enforcement of the Code, including all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue. Providing a regulatory definition of interest for purposes of section 163(j) and the anti-avoidance rule falls within this authority. The statutory language of section 163(j)(1) (''The amount allowed as a deduction *under this chapter* for any taxable year for business interest . . .'') (emphasis added) also supports the application of section 163(j) to more items than merely items traditionally deducted under section 163(a).

Although the Treasury Department and the IRS have the authority to prescribe regulations addressing interest equivalents and anti-avoidance transactions, as noted earlier in parts II(E)(3) and (4) of this Summary of Comments and Explanation of Revisions section, in response to comments, the final regulations nevertheless limit the interest equivalent items to those items commenters agreed should be treated as interest expense or interest income, substitute interest payments made in connection with a sale-repurchase agreement or securities lending transaction that is not entered into by the taxpayer in the taxpayer's ordinary course of business, and certain amounts relating to transaction(s) entered into by a taxpayer with a principal purpose of artificially reducing interest expense or increasing interest income.

F. Definition of Motor Vehicle—Proposed § 1.163(j)–1(b)(25)

Proposed § 1.163(j)–1(b)(25) provides that the term ''motor vehicle'' means a motor vehicle as defined in section 163(j)(9)(C). Under section 163(j)(9)(C), a motor vehicle means any self-propelled vehicle designed for transporting persons or property on a public street, highway, or road; a boat; and farm machinery or equipment. A few commenters questioned whether towed recreational vehicles and trailers are included in the definition of ''motor vehicle.'' One commenter requested that the final regulations define motor vehicle to include any trailer or camper that is designed to provide temporary living quarters for recreational, camping, travel, or seasonal use and is designed to be towed by, or affixed to, a motor vehicle. Another commenter recommended allowing motor vehicle dealers to deduct floor plan financing interest on both motor vehicles and trailers that are offered for sale in integrated or related businesses.

Because section 163(j)(9)(C) specifically defines motor vehicles as self-propelled vehicles, the Treasury Department and the IRS do not have the authority to expand the definition of motor vehicles in the final regulations to include vehicles that are not self-propelled, such as towed recreational vehicles and trailers. For this reason, the Treasury Department and the IRS decline to adopt these comments in the final regulations. Therefore, the definition of motor vehicles in the final regulations continues to incorporate the definition in section 163(j)(9)(C) by cross-reference.

G. Definition of Taxable Income—Proposed § 1.163(j)–1(b)(37)

1. Calculation of Taxable Income

Proposed § 1.163(j)–1(b)(1)(i)(A) provides that business interest expense is added to taxable income to determine ATI. Some commenters noted that this provision could be construed as distorting ATI if a taxpayer has a disallowed business interest expense carryforward from a prior taxable year. Under such facts, the proposed regulations would not have reduced taxable income by the amount of the carryforward, because proposed § 1.163(j)–1(b)(37) disregards the carryforward as part of section 163(j) and the section 163(j) regulations. However, in calculating ATI, taxpayers might argue that taxable income should be increased by the amount of the disallowed business interest expense carryforward because the term ''business interest expense'' in the proposed regulations includes disallowed business interest expense carryforwards.

The Treasury Department and the IRS did not intend to create a net positive adjustment to ATI for disallowed business interest expense carryforwards. To address this potential distortion, the final regulations clarify that tentative taxable income is computed without regard to the section 163(j) limitation, and that disallowed business interest expense carryforwards are not added to tentative taxable income in computing ATI under § 1.163(j)–1(b)(1).

2. Interaction With Section 250

Proposed § 1.163(j)–1(b)(37)(ii) provides a rule to coordinate the application of sections 163(j) and 250. Section 250(a)(1) generally provides a deduction based on the amount of a domestic corporation's foreign-derived intangible income and GILTI. Section 250(a)(2) limits the amount of this deduction based on the taxpayer's taxable income—the greater the amount of a taxpayer's taxable income for purposes of section 250(a)(2), the greater the amount of the taxpayer's allowable deduction under section 250(a)(1).

In particular, proposed § 1.163(j)–1(b)(37)(ii) provides that, if a taxpayer is allowed a deduction for a taxable year under section 250(a)(1) that is properly allocable to a non-excepted trade or business, then the taxpayer's taxable income for that year is determined without regard to the limitation in section 250(a)(2). Some commenters observed that this proposed rule results in a lower ATI and section 163(j) limitation for the taxpayer than if the limitation in section 250(a)(2) were taken into account. Commenters also stated that the rationale for this approach (which does not reflect the taxpayer's actual taxable income) is unclear, and they recommended that this provision be withdrawn or made elective for taxpayers.

The Treasury Department and the IRS have determined that further study is required to determine the appropriate rule for coordinating sections 250(a)(2), 163(j), and other Code provisions (such as sections 170(b)(2) and 172(a)(2)) that limit the availability of deductions based, directly or indirectly, upon a taxpayer's taxable income (taxable income-based provisions). Therefore, the final regulations do not contain the rule in proposed § 1.163(j)–1(b)(37)(ii). Until such additional guidance is effective, taxpayers may choose any reasonable approach (which could include an ordering rule or the use of simultaneous equations) for coordinating taxable income-based provisions as long as such approach is applied consistently for all relevant taxable years. For this purpose, the ordering rule contained in proposed §§ 1.163(j)–1(b)(37)(ii) (83 FR 67490 (Dec. 28, 2018)) and 1.250(a)–1(c)(4) (contained in 84 FR 8188 (March 6, 2019)) is treated as a reasonable approach for coordinating sections 163(j) and 250. Comments are welcome on what rules should be provided, and whether an option to use simultaneous equations in lieu of an ordering rule would be appropriate in order to coordinate taxable income-based provisions.

3. When Disallowed Business Interest Expense Is ''Paid or Accrued''

As noted in the Background section of this preamble, section 163(j)(2) provides that the amount of any business interest not allowed as a deduction for any taxable year under section 163(j)(1) is treated as business interest ''paid or accrued'' in the succeeding taxable year. Commenters asked for clarification as to whether disallowed business interest expense should be treated as ''paid or accrued'' in the taxable year in which such expense is taken into account for Federal income tax purposes (without regard to section 163(j)), or whether such expense instead should be treated as paid or accrued in the succeeding taxable year in which the expense can be deducted by the taxpayer under section 163(j).

For purposes of section 163(j) and the section 163(j) regulations, the term ''paid or accrued'' in section 163(j)(2) must be construed in such a way as to further congressional intent. Although the use of this term in section 163(j)(2) provides a mechanism for disallowed business interest expense to be carried forward to and deducted in a subsequent taxable year, it does not mean that a disallowed business interest expense carryforward is treated as paid or accrued in a subsequent year for all purposes. In certain contexts, a disallowed business interest expense must be treated as paid or accrued in the year the expense was paid or accrued without regard to section 163(j) to give effect to congressional intent. For example, if a disallowed business interest expense were treated as paid or accrued only in a future taxable year in which such expense could be deducted after the application of section 163(j), then section 382 never would apply to such expense (because disallowed business interest expense carryforwards never would be pre-change losses). This outcome is clearly contrary to congressional intent (see section 382(d)(3)). Similarly, if a disallowed business interest expense were treated as paid or accrued in a future taxable year for purposes of section 163(j)(8)(A)(ii), then such expense would be added back to tentative taxable income in determining ATI for that taxable year (and for all future taxable years to which such expense is carried forward under section 163(j)(2)), thereby artificially increasing the taxpayer's section 163(j) limitation. (See part II(A) of this Summary of Comments and Explanation of Revisions section.) This outcome also is inconsistent with congressional intent. However, in other contexts, a disallowed business interest expense must be treated as paid or accrued in a succeeding taxable year to allow for the deduction of the carryforward in that year.

The definition of ''disallowed business interest expense'' has been revised in the final regulations to reflect that, solely for purposes of section 163(j) and the section 163(j) regulations, disallowed business interest expense is treated as ''paid or accrued'' in the taxable year in which the expense is taken into account for Federal income tax purposes (without regard to section 163(j)), or in a succeeding taxable year in which the expense can be deducted by the taxpayer under section 163(j), as the context may require.

4. Interaction With Sections 461(l), 465, and 469—Proposed § 1.163(j)–1(b)(37)

The Treasury Department and the IRS received questions asking for clarification of the interaction between proposed § 1.163(j)–1(b)(37) and the limitations in sections 461(l), 465, and 469. The final regulations clarify that sections 461(l), 465, and 469 are taken into account when determining tentative taxable income. Then, as provided in proposed § 1.163(j)–3(b)(4), sections 461(l), 465, and 469 are applied after the application of the section 163(j) limitation. See part II(B) of this Summary of Comments and Explanation of Revisions section.

H. Definition of Trade or Business—Proposed § 1.163(j)–1(b)(38)

1. In General

The section 163(j) limitation applies to taxpayers with ''business interest,'' which is defined in section 163(j)(5) as any interest properly allocable to a trade or business. Neither section 163(j) nor the legislative history defines the term ''trade or business.'' However, section 163(j)(7) provides that the term ''trade or business'' does not include the trade or business of performing services as an employee, as well as electing real property, electing farming, and certain utility trades or businesses.

As described in the preamble to the proposed regulations, the proposed regulations define the term ''trade or business'' by reference to section 162. Section 162(a) permits a deduction for all the ordinary and necessary expenses paid or incurred in carrying on a trade or business. Commenters requested additional guidance in determining whether an activity constitutes a section 162 trade or business.

The rules under section 162 for determining the existence of a trade or business are well-established and illustrated through a large body of case law and administrative guidance. Additionally, whether an activity is a section 162 trade or business is inherently a factual question. *Higgins* v. *Commissioner,* 312 U.S. 212, 217 (1941) (determining ''whether the activities of a taxpayer are 'carrying on a business' requires an examination of the facts in each case'').

The courts have developed two definitional requirements. One, in relation to profit motive, requires the taxpayer to enter into and carry on the activity with a good-faith intention to make a profit or with the belief that a profit can be made from the activity. The second, in relation to the scope of the activities, requires considerable, regular, and continuous activity. See generally *Commissioner* v. *Groetzinger,* 480 U.S. 23 (1987). In the seminal case of *Groetzinger,* the Supreme Court stated that, ''[w]e do not overrule or cut back on the Court's holding in *Higgins* when we conclude that if one's gambling activity is pursued full time, in good faith, and with regularity, to the production of income for a livelihood, and is not a mere hobby, it is a trade or business within the meaning of the statutes with which we are here concerned.'' Id. at 35.

2. Multiple Trades or Businesses Within an Entity

Commenters also suggested there should be factors to determine how to delineate separate section 162 trades or businesses within an entity and when an entity's combined activities should be considered a single section 162 trade or business for purposes of section 163(j). One commenter suggested adopting the rules for separate trades or businesses provided in section 446 and the regulations thereunder.

The Treasury Department and the IRS decline to adopt these recommendations because specific guidance under section 162 is beyond the scope of the final regulations. Further, § 1.446–1(d) does not provide guidance on when trades or businesses will be considered separate and distinct. Instead, it provides that a taxpayer may use different methods of accounting for separate and distinct trades or businesses, and it specifies two circumstances in which trades or businesses will not be considered separate and distinct. For example, § 1.446–1(d)(2) provides that no trade or business will be considered separate and distinct unless a complete and separable set of books and records is kept for such trade or business.

The Treasury Department and the IRS recognize that an entity can conduct more than one trade or business under section 162. This position is inherent in the allocation rules detailed in proposed § 1.163(j)–10(c)(3), which require a taxpayer with an asset used in more than one trade or business to allocate its adjusted basis in the asset to each trade or business using the permissible methodology described therein. In this context, the final regulations provide, consistent with the proposed regulations, that maintaining separate books and records for all excepted and non-excepted trades or businesses is one indication that a particular asset is used in a particular trade or business.

Whether an entity has multiple trades or businesses is a factual determination, and numerous court decisions that define the meaning of ''trade or business'' also provide taxpayers guidance in determining whether more than one trade or business exists. See *Groetzinger,* 480 U.S. at 35. For example, some court decisions discuss whether the activities have separate books and records, facilities, locations, employees, management, and capital structures, and whether the activities are housed in separate legal entities.

Accordingly, the final regulations define ''trade or business'' as a trade or business within the meaning of section 162, which should aid taxpayers in the proper allocation of interest expense, interest income, and other tax items to a trade or business and to an excepted or non-excepted trade or business.

3. Rental Real Estate Activities as a Trade or Business

See the discussion of elections for real property trades or businesses that may not qualify as section 162 trades or businesses in part X of this Summary of Comments and Explanation of Revisions section.

4. Separate Entities

One commenter requested clarification that the determination of whether an entity generates interest attributable to a trade or business within the meaning of section 162 is made at the entity level without regard to the classification of the entity's owners. Except in the context of a consolidated group, or if § 1.163(j)–10 provides otherwise, the determination of whether an entity generates interest and whether such interest is properly allocable to a trade or business is determined at the entity level, without regard to the classification of the entity's owners. See also the discussion of trading partnerships and CFC groups in the Concurrent NPRM.

I. Applicability Dates

The proposed regulations provide generally that the final regulations would apply to taxable years ending after the date that this Treasury Decision is published in the **Federal Register**. The proposed applicability date has been changed in the final regulations to avoid the application of the changes reflected in the final regulations to a taxpayer at the end of the taxable year, which may result in unexpected effects on the taxpayer under section 163(j). Accordingly, the final regulations generally apply to taxable years beginning on or after the date that is 60 days after the date that this Treasury Decision is published in the **Federal Register**.

III. Comments on and Changes to Proposed § 1.163(j)–2: Deduction for Business Interest Expense Limited

Proposed § 1.163(j)–2 provides general rules regarding the section 163(j) limitation, including rules on how to calculate the limitation, how to treat disallowed business interest expense carryforwards, and how the small business exemption and the aggregation rules apply with the limitation. The following discussion addresses comments relating to proposed § 1.163(j)–2.

A. Whether the Section 163(j) Limitation Is a Method of Accounting

A few commenters requested clarification that the section 163(j) limitation is not a method of accounting under section 446 and the regulations thereunder. The commenters requested clarification on whether the application of the section 163(j) limitation is a method of accounting because the rules under section 163(j) appear to defer, rather than permanently disallow, a deduction for disallowed business interest expense and disallowed disqualified interest (as defined in proposed § 1.163(j)–1(b)(10)). Specifically, section 163(j)(2) and proposed § 1.163(j)–2(c) allow the carryforward of disallowed business interest expense, and proposed § 1.163(j)–2(c) allows the carryforward of disallowed disqualified interest, to succeeding taxable years.

Section 1.446–1(a)(1) defines the term ''method of accounting'' to include not only the overall method of accounting of a taxpayer, but also the accounting treatment of any item of gross income or deduction. Under § 1.446–1(e)(2)(ii)(*a*), an accounting method change includes a change in the overall plan of accounting for gross income or deductions or a change in the treatment of any material item used in such overall plan of accounting. Moreover, § 1.446–1(e)(2)(ii)(*a*) provides that a ''material item'' is any item that involves the proper time for the inclusion of the item in income or the taking of a deduction. The key characteristic of a material item ''is that it determines the timing of income or deductions.'' *Knight-Ridder Newspapers, Inc.* v. *United States,* 743 F.2d 781, 798 (11th Cir. 1984). Once a taxpayer has established a method of accounting for an item of income or expense, the taxpayer must obtain the consent of the Commissioner under section 446(e) before changing to a different method of accounting for that item.

For purposes of § 1.446–1(e)(2)(ii)(*a*), if there is a change in the application of the section 163(j) limitation, the item involved is the taxpayer's deduction for business interest expense. The taxpayer is not changing its treatment of this item; instead, the taxpayer is changing the limitation placed upon that specific item. The effect of removing the section 163(j) limitation is that the taxpayer would be able to recognize the full amount of the interest expense that is otherwise deductible under its accounting method in a given taxable year before it was limited by section 163(j).

The Treasury Department and the IRS do not view the section 163(j) limitation as a method of accounting under section 446(e) and the regulations thereunder. The determination of whether a taxpayer is subject to the section 163(j) limitation is determined for each taxable year. The carryover rules in section 163(j)(2) and proposed § 1.163(j)–2(c) provide that disallowed business interest expense and disallowed disqualified interest may be carried forward to a future taxable year. However, section 163(j) does not provide a mechanism to ensure that, in every situation, a taxpayer will be able to deduct the business interest expense that the taxpayer was not permitted to deduct in one taxable year and was required to carry forward to succeeding taxable years. Thus, the section 163(j) limitation is not a method of accounting under § 1.446–1(e)(2)(ii)(*a*) because the change in practice may result in a permanent change in the taxpayer's lifetime taxable income. Further, the section 163(j) limitation does not involve an ''item'' as it is not a recurring element of income or expense.

B. General Gross Receipts Test and Aggregation

As noted in the preamble to the proposed regulations, section 163(j)(3) exempts certain small businesses from the section 163(j) limitation. See proposed § 1.163(j)–2(d). Under section 163(j), a small business taxpayer is one that meets the gross receipts test in section 448(c) and is not a tax shelter under section 448(a)(3). The gross receipts test is met if a taxpayer has average annual gross receipts for the three taxable years prior to the current taxable year of $25 million or less. For taxable years beginning after December 31, 2018, the gross receipts threshold reflects an annual adjustment for inflation as provided for in section 448(c)(4); thus, the gross receipts threshold for taxable years beginning in 2020 is $26 million. See section 3.31 of Rev. Proc. 2019–44, 2019–47 I.R.B.1093. Section 448(c)(2) aggregates the gross receipts of multiple taxpayers that are treated as a single employer under sections 52(a) and (b) and 414(m) and (o). The gross receipts test under section 448(c) normally applies only to corporations and to partnerships with C corporation partners. However, section 163(j)(3) and proposed § 1.163(j)–2(d)(2)(i) provide that, for a taxpayer that is not a corporation or a partnership, the gross receipts test of section 448(c) applies as if the taxpayer were a corporation or a partnership.

Some commenters noted that the aggregation rules in sections 52(a) and (b) and sections 414(m) and (o) could be difficult to apply in certain instances due to their complexity. Other commenters asked that the final regulations clarify the application of the aggregation rules to the gross receipts test under section 448(c). Addressing the application of the aggregation rules to the gross receipts test is beyond the scope of the final regulations. The section 52(a) and (b) aggregation rules were enacted as part of the work opportunity tax credit, but have also been applied to numerous Code provisions, including sections 45A, 45S, 264, 280C and 448. The affiliated service group rules under section 414(m) were enacted to address certain abuses related to qualified retirement plans, but also have been applied to several other Code provisions, including sections 45R, 162(m), 414(t), 4980H, and 4980I.

However, the Treasury Department and the IRS are aware that the aggregation rules set forth in sections 52(a) and (b) and sections 414(m) and (o) are complex. Therefore, Frequently Asked Questions that explain the basic operation of these rules are provided on *http://irs.gov/newsroom.* See FAQs Regarding the Aggregation Rules Under Section 448(c)(2) that Apply to the Section 163(j) Small Business Exemption. The Treasury Department and the IRS continue to study the application of the aggregation rules to the gross receipts test, and request comments on issues relating to such application, taking into account the application of the aggregation rules beyond the gross receipts test.

The Treasury Department and the IRS continue to review and consider issues relating to the affiliated service group rules under section 414(m), and a guidance project regarding the aggregation rules under section 414(m) is listed on the 2019–2020 Priority Guidance Plan (RIN 1545–BO34). As guidance is published relating to the affiliated service group rules, the FAQs will be updated, taking into account the various Code provisions to which these aggregation rules apply.

In addition, the Treasury Department and the IRS recognize that proposed § 1.163(j)–2(d)(2)(i) may generate confusion with respect to the aggregation rules. Although section 448(c) applies only to corporations and to partnerships with a C corporation partner, sections 52(a), 52(b), 414(m), and 414(o) apply to a broader array of entities. These statutes contain different ownership thresholds for different types of entities that apply in determining whether multiple entities are treated as a single employer. To resolve potential confusion, the final regulations remove the reference to the aggregation rules from proposed § 1.163(j)–2(d)(2)(i). Taxpayers that are not a corporation or a partnership with a C corporation partner must apply section 448(c) as if they were a corporation or a partnership in accordance with section 163(j)(3) and proposed § 1.163(j)–2(d)(2)(i). However, taxpayers should treat themselves as the type of entity that they actually are in applying sections 52(a), 52(b), 414(m), and 414(o).

C. Small Business Exemption and Single Employer Aggregation Rules—Proposed §§ 1.163(j)–2(d) and 1.52–1(d)(1)(i)

Section 52(b) treats trades or businesses under common control as a single employer. Section 1.52–1(b) through (d) defines ''trades or businesses under common control'' to include parent-subsidiary groups and brother-sister groups. Commenters noted that the version of § 1.52–1(d)(1)(i) in effect at the time of the proposed regulations defined ''brother-sister groups'' to include entities a controlling interest in which is owned by the same 5 or fewer people who are individuals, estates, or trusts (directly and with the application of § 1.414(c)–4(b)(1)).

Section 1.414(c)–4(b)(1) provides that, if a person has an option to purchase an interest in an organization, the person is deemed to own an interest in that organization. Other provisions under § 1.414(c)–4 apply attribution on a broader scale, such as through familial relationships and for closely held partnerships and S corporations.

Commenters questioned whether the cross-reference in § 1.52–1(d)(1)(i) was correct, and whether the cross-reference should have been to § 1.414(c)–4 instead of § 1.414(c)–4(b)(1). The Treasury Department and the IRS agree that there is no discernible reason why § 1.52–1(d)(1)(i) aggregation should be limited solely to options holders. Taxpayers need to know how to aggregate gross receipts properly in order to know if they are subject to section 163(j).

On July 11, 2019, a correcting amendment to T.D. 8179 was published in the **Federal Register** to clarify that the cross-reference in § 1.52–1(d)(1)(i) should be to § 1.414(c)–4. See 84 FR 33002. This correcting amendment should eliminate uncertainty for taxpayers that need to determine how to aggregate gross receipts in the context of a brother-sister group under common control.

D. Small Business Exemption and Tax Shelters—Proposed § 1.163(j)–2(d)(1)

Consistent with section 163(j)(3), proposed § 1.163(j)–2(d)(1) provides that the exemption for certain small businesses that meet the gross receipts test of section 448(c) does not apply to a tax shelter as defined in section 448(d)(3). Several commenters requested clarification on the application of the small business exemption under section 163(j)(3) to a tax shelter.

Section 448(d)(3) defines a tax shelter by cross-reference to section 461(i)(3), which defines a tax shelter, in relevant part, as a syndicate within the meaning of section 1256(e)(3)(B). Section 1.448–1T(b)(3) provides, in part, that a syndicate is a partnership or other entity (other than a C corporation) if more than 35 percent of its losses during the taxable year are *allocated* to limited partners or limited entrepreneurs, whereas section 1256(e)(3)(B) refers to losses that are *allocable* to limited partners or limited entrepreneurs. As a result, the scope of the small business exemption in section 163(j)(3) is unclear. Commenters requested that an entity be a syndicate in a taxable year only if it has net losses in that year and more than 35 percent of those net losses are actually *allocated* to limited partners or limited entrepreneurs. To provide a consistent definition of the term ''syndicate'' for purposes of sections 163(j), 448, and 1256, the Treasury Department and the IRS propose to define the term ''syndicate'' using the actual allocation rule from the definition in § 1.448–1T(b)(3). This definition is also consistent with the definition used in a number of private letter rulings under section 1256. See proposed § 1.1256(e)–2(a) in the Concurrent NPRM.

Commenters also requested specific relief for small business taxpayers from the definition of a syndicate based on the ''active management'' exception under section 1256(e)(3)(C). Section 1256(e)(3)(C) lists several examples of interests in an entity that ''shall not be treated as held by a limited partner or a limited entrepreneur,'' thus excluding the entity from the definition of a syndicate. In particular, section 1256(e)(3)(C)(v) allows the Secretary to determine (by regulations or otherwise) ''that such interest should be treated as held by an individual who actively participates in the management of such entity, and that such entity and such interest are not used (or to be used) for tax-avoidance purposes.''

The commenters requested that the Treasury Department use its authority under section 1256(e)(3)(C)(v) to provide relief from the definition of a syndicate to small business entities that (1) qualify under the gross receipts test of section 448(c), (2) meet the definition of a syndicate, and (3) do not qualify to make an election as an electing real property business or electing farming business. If a small business satisfies these three conditions, the commenters requested that the Treasury Department and the IRS provide a rule that all interests in the entity are treated as held by partners or owners who actively participate in the management of such entity.

The Treasury Department and the IRS have determined that the request deeming limited partners in small partnerships to be active participants even if those owners would not be treated as active participants under section 1256(e)(3)(C) is contrary to the statutory language and legislative history in section 163(j)(3). Therefore, the Treasury Department and the IRS decline to adopt the comments.

Another commenter asked for clarification on how to compute the amount of loss to be tested under § 1.448–1T(b)(3) and section 1256(e)(3)(B). The commenter provided a particular fact pattern in which a small business would be caught in an iterative loop of (a) of having net losses due to a business interest deduction, (b) which would trigger disallowance of the exemption for small businesses in section 163(j)(3) if more than 35 percent of the losses were allocated to a limited partner, (c) which would trigger the application of the section 163(j)(1) limitation to reduce the amount of the interest deduction, (d) which would then lead to the taxpayer having no net losses and therefore being eligible for the application of the exemption for small businesses under section 163(j)(3). To address this fact pattern, in the Concurrent NPRM, the Treasury Department and the IRS have added an ordering rule providing that, for purposes of section 1256(e)(3)(B) and § 1.448–1T(b)(3), losses are determined without regard to section 163(j). See proposed § 1.1256(e)–2(b) and the example provided in proposed § 1.1256(e)–2(c) in the Concurrent NPRM.

E. Gross Receipts for Partners in Partnerships and Shareholders of S Corporation Stock—Proposed § 1.163(j)–2(d)(2)(iii)

Proposed § 1.163(j)–2(d)(iii) provides that, in determining whether a taxpayer meets the gross receipts test of section 448(c), each partner in a partnership includes a share of partnership gross receipts in proportion to such partner's distributive share of items of gross income that were taken into account by the partnership under section 703. Similarly, shareholders of S corporations include a pro rata share of the S corporation's gross receipts. See Rev. Rul. 71–455, 1971–2 C.B. 318 (holding that a partner's distributive share of the partnership's gross receipts is used in applying the passive investment income test under section 1372(e)(5)).

This approach would be applicable only in situations in which the partner and the partnership (or a shareholder and the S corporation) are not treated as one person under the aggregation rules of sections 52(a) and (b) and 414(m) and (o). The Treasury Department and the IRS requested comments in the preamble to the proposed regulations on this approach and on whether other approaches to determining the gross receipts of partners and S corporation shareholders for purposes of section 163(j) would measure the gross receipts of such partners and shareholders more accurately.

In response, several commenters suggested different approaches for determining the gross receipts of partners and S corporation shareholders. One commenter recommended that a taxpayer should include gross receipts only from entities eligible for the small business exemption (exempt entities). In other words, the commenter recommended that a taxpayer's gross receipts should not include gross receipts from (1) any electing real property trade or business or electing farming business; (2) any entities utilizing the floor plan financing interest exception under section 163(j)(1)(C); and (3) any other entities subject to section 163(j). The commenter noted that this modification would simplify the computation of gross receipts and prevent the same gross receipts from being double-counted both at the entity level and the partner or S corporation shareholder level. However, the determination of gross receipts generally is not affected by whether any other entity is subject to section 163(j).

One commenter noted that passthrough entities generally do not provide information regarding gross receipts to their partners. As it is difficult for partners to determine the partnership's gross receipts, the commenter suggested various approaches, such as a de minimis rule whereby a less-than-10 percent owner of a passthrough entity may use the taxable income from such entity rather than gross receipts; use the current-year gross receipts as a reasonable estimate of the past three years; or not exclude the gross receipts of the exempt entity in certain situations.

Another commenter recommended that, in situations in which a partner and a partnership are not subject to the aggregation rules of section 448(c), a partner should not be required to include any share of partnership gross receipts when determining its partner-level eligibility for the small business exemption. The commenter noted that section 163(j) is applied at the partnership level. The commenter stated it is inconsistent to take an aggregate view of partnerships for purposes of the small business exemption without a specific rule under section 163(j) requiring such attribution or aggregation. The commenter also stated that requiring a partner to include a share of partnership gross receipts would discourage taxpayers who operate small businesses from investing in partnerships.

The Treasury Department and the IRS understand that passthrough entities might not have reported gross receipts to their partners or shareholders in the past. However, the statute is clear that a taxpayer must meet the gross receipts test of section 448(c), and that, if the taxpayer is not subject to section 448(c), the section 448(c) rules must be applied in the same manner as if such taxpayer were a corporation or partnership. The alternatives presented either do not have universal application or do not adequately reflect a passthrough entity's gross receipts.

Additionally, there is no authority under section 448 and the regulations thereunder to substitute taxable income for gross receipts or to estimate gross receipts. Accordingly, the Treasury Department and the IRS do not adopt the suggested approaches, and the proposed rules are finalized without any change.

IV. Comments on and Changes to Section Proposed § 1.163(j)–3: Relationship of Section 163(j) Limitation to Other Provisions Affecting Interest

Proposed § 1.163(j)–3 provides ordering and operating rules that control the interaction of the section 163(j) limitation with other provisions of the Code that defer, capitalize or disallow interest expense. The ordering and operating rules provide that section 163(j) applies before the operation of the loss limitation rules in section 465 and 469, and before the application of section 461(l), and after other provisions of the Code that defer, capitalize, or disallow interest expense. The ordering and operating rules in proposed § 1.163(j)–3 apply only in determining the amount of interest expense that could be deducted without regard to the section 163(j) limitation, and not for other purposes, such as the calculation of ATI. The following discussion addresses comments relating to proposed § 1.163(j)–3.

A. Capitalized Interest

Proposed § 1.163(j)–3(b)(5) provides that provisions that require interest to be capitalized, such as sections 263A and 263(g), apply before section 163(j). Commenters suggested that this section is too restrictive by referring solely to sections 263(A) and 263(g), and that other provisions could require interest to be capitalized. The Treasury Department and the IRS agree with this comment, and an appropriate revision has been made in the final regulations to account for any possible additional provisions that could require interest to be capitalized.

B. Provisions That Characterize Interest Expense as Something Other Than Business Interest Expense

Proposed § 1.163(j)–3(b)(9) generally provides that provisions requiring interest expense to be treated as something other than business interest expense, such as section 163(d) governing investment interest expense, govern the treatment of the interest expense. Commenters expressed confusion with the provision, suggesting that, by virtue of the statute and the proposed regulations, if interest expense is treated as something other than business interest expense, there is no need to consult proposed § 1.163(j)–3. The Treasury Department and the IRS generally agree with the comment and have removed this section from the final regulations.

C. Section 108

In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments on the interaction between section 163(j) and the rules addressing income from the discharge of indebtedness under section 108. In response, commenters noted, for example, that it is unclear whether cancellation of indebtedness income under section 61(a)(11) arises when the taxpayer only receives a benefit in the form of a disallowed business interest expense carryforward, or whether any exclusions, such as sections 108(e)(2) or 111, or any tax benefit principles, should apply. In light of the complex and novel issues raised in these comments, the Treasury Department and the IRS have determined that the interaction between section 163(j) and section 108 requires further consideration and may be the subject of future guidance.

D. Sections 461(l), 465, and 469

The proposed regulations provide that sections 461(l), 465, and 469 apply after the application of section 163(j). The Treasury Department and the IRS received informal questions about the effect of these sections on the calculation of ATI. Therefore, the final regulations clarify whether and how sections 461(l), 465, and 469 are applied when determining tentative taxable income. The final regulations also include examples to demonstrate the calculation of ATI if a loss tentatively is suspended in the calculation of tentative taxable income, and if a loss is carried forward from a prior taxable year under section 469.

V. Comments on and Changes to Proposed § 1.163(j)–4: General Rules Applicable to C Corporations (Including Real Estate Investment Trusts (REITs), RICs, and Members of Consolidated Groups) and Tax-Exempt Corporations

Section 1.163(j)–4 provides rules regarding the computation of items of income and expense under section 163(j) for taxpayers that are C corporations (including members of a consolidated group, REITs, and RICs) and tax-exempt corporations. The following discussion addresses comments relating to proposed § 1.163(j)–4.

A. Aggregating Affiliated but Non-Consolidated Entities

Under the proposed regulations, members of a consolidated group are aggregated for purposes of section 163(j), and the consolidated group has a single section 163(j) limitation. In contrast, partnerships that are wholly owned by members of a consolidated group are not aggregated with the group for purposes of section 163(j), and members of an affiliated group that do not file a consolidated return are not aggregated with each other for purposes of section 163(j).

Several commenters recommended that aggregation rules be applied to related taxpayers other than consolidated group members. For example, one commenter recommended that aggregation rules similar to those provided under section 199A be applied for purposes of the section 163(j) limitation to obviate the need for related entities to shift debt or business assets around to avoid this limitation. Several other commenters noted that the 1991 Proposed Regulations applied section 163(j) to an affiliated group of corporations (including all domestic corporations controlled by the same parent, whether consolidated or not) and recommended that this ‘‘super-affiliation rule’’ be retained so that affiliated but non-consolidated groups are not disadvantaged under the section 163(j) regulations. In contrast, another commenter agreed with the approach taken in the proposed regulations with respect to affiliated but non-consolidated groups, in part because the allocation of the section 163(j) limitation among non-consolidated affiliates can become quite complex.

Commenters also recommended that a partnership owned by members of an affiliated group (controlled partnership) be treated as an aggregate rather than an entity so that the section 163(j) limitation would not apply separately at the partnership level. Instead, each partner would include its allocable share of the controlled partnership's tax items in determining its own section 163(j) limitation, and transactions between the controlled partnership and its controlling partners would be disregarded. Some commenters would apply this approach to partnerships wholly owned by members of a controlled group of corporations (as defined in section 1563). Others would apply this approach to partnerships wholly owned (or at least 80 percent-owned) by members of a consolidated group in order to reduce compliance complexity, to ensure that similarly situated taxpayers (namely, consolidated groups that conduct business activities directly and those that conduct such activities through a controlled partnership) are treated similarly, and to discourage consolidated groups from creating a controlled partnership to obtain a better result under section 163(j). Commenters observed that the proposed regulations apply an aggregate approach to certain controlled partnerships that own CFCs (see proposed § 1.163(j)–7(f)(6)(ii)(B)), and they recommended applying this principle more broadly.

As explained in the preamble to the proposed regulations, the Treasury Department and the IRS have determined that non-consolidated entities generally should not be aggregated for purposes of applying the section 163(j) limitation. Whereas old section 163(j)(6)(C) expressly provided that ''[a]ll members of the same affiliated group (within the meaning of section 1504(a)) shall be treated as 1 taxpayer,'' section 163(j) no longer contains such language, and nothing in the legislative history of section 163(j) suggests that Congress intended non-consolidated entities to be treated as a single taxpayer for purposes of section 163(j). See the Concurrent NPRM for a discussion of a proposed exception to this general rule for CFCs. Moreover, the Treasury Department and the IRS have determined that controlled partnerships generally should not be treated as aggregates because section 163(j) clearly applies at the partnership level. See section 163(j)(4). In other words, Congress decided that partnerships should be treated as entities rather than aggregates for purposes of section 163(j). Additionally, revising the regulations to treat controlled partnerships as aggregates would not necessarily achieve the objectives sought by commenters because the controlling partners effectively could ''elect'' entity or aggregate treatment for the partnership simply by selling or acquiring interests therein (thereby causing the partnership to satisfy or fail the ownership requirement for aggregate treatment).

However, the Treasury Department and the IRS are concerned that the application of section 163(j) on an entity-by-entity basis outside the consolidated group context could create the potential for abuse in certain situations by facilitating the separation of excepted and non-excepted trades or businesses. For example, a consolidated group that is engaged in both excepted and non-excepted trades or businesses could transfer its excepted trades or businesses to a controlled partnership, which in turn could borrow funds from a third party and distribute those funds to the consolidated group tax-free under section 731 (unless the debt is recharacterized as debt of the consolidated group in substance; see *Plantation Patterns, Inc.* v. *Commissioner,* 462 F.2d 712 (5th Cir. 1972)). Similarly, an individual taxpayer that is engaged in both excepted and non-excepted trades or businesses could transfer its excepted trades or businesses to a controlled corporation, which in turn could borrow funds from a third party and distribute those funds to the individual tax-free under section 301(c)(2) (assuming the corporation has no earnings and profits). Additionally, a partnership with two trades or businesses—one that generates ATI, and another that generates losses—could separate the two trades or businesses into a tiered partnership structure solely for the purpose of borrowing through the partnership that generates ATI and avoiding a section 163(j) limitation.

The anti-avoidance rule in proposed § 1.163(j)–2(h) and the anti-abuse rule in proposed § 1.163(j)–10(c)(8) would preclude taxpayers from undertaking the foregoing transfers in certain circumstances. The final regulations add an example illustrating the application of the anti-avoidance rule in proposed § 1.163(j)–2(h) to the use of a controlled corporation to avoid the section 163(j) limitation, as well as an example illustrating the application of this anti-avoidance rule to the use of a lower-tier partnership to avoid the section 163(j) limitation in a similar manner.

Commenters further requested that the Treasury Department and the IRS simplify the rules applicable to controlled partnerships if the final regulations do not treat such partnerships as aggregates rather than entities. For example, commenters recommended (i) eliminating steps 3 through 10 in proposed § 1.163(j)–6(f)(2) for such partnerships, (ii) applying the principles of the § 1.469–7 self-charged interest rules to partnership interest expense and income owed to or from consolidated group members by treating all members of the group as a single taxpayer, or (iii) allowing excess taxable income (ETI) that is allocated by a partnership to one consolidated group member to offset excess business interest expense allocated by that partnership to another group member.

The final regulations do not adopt these recommendations. For a discussion of steps 3 through 10 in proposed § 1.163(j)–6(f)(2), see part VII(A)(3) of this Summary of Comments and Explanation of Revisions section. For a discussion of the self-charged interest rules, see the Concurrent NPRM. For a discussion of the proposal to allow ETI allocated by a partnership to one member of a consolidated group to offset excess business interest expense allocated by that partnership to another group member, see part V(D)(4) of this Summary of Comments and Explanation of Revisions section.

B. Intercompany Transactions and Intercompany Obligations

Proposed § 1.163(j)–4(d)(2) contains rules governing the calculation of the section 163(j) limitation for members of a consolidated group. These rules provide, in part, that: (i) A consolidated group has a single section 163(j) limitation; (ii) for purposes of calculating the group's ATI, the relevant taxable income is the consolidated group's consolidated taxable income, and intercompany items and corresponding items are disregarded to the extent they offset in amount; and (iii) for purposes of calculating the group's ATI and determining the business interest expense and business interest income of each member, all intercompany obligations (as defined in § 1.1502–13(g)(2)(ii)) are disregarded (thus, interest expense and interest income from intercompany obligations are not treated as business interest expense and business interest income for purposes of section 163(j)).

In turn, proposed § 1.163(j)–5(b)(3) contains rules governing the treatment of disallowed business interest expense carryforwards for consolidated groups. These rules provide, in part, that if the aggregate amount of members' business interest expense (including disallowed business interest expense carryforwards) exceeds the group's section 163(j) limitation, then: (i) Each member with current-year business interest expense and either current-year business interest income or floor plan financing interest expense deducts current-year business interest expense to the extent of its current-year business interest income and floor plan financing interest expense; (ii) if the group has any remaining section 163(j) limitation, each member with remaining current-year business interest expense deducts a pro rata portion of its expense; (iii) if the group has any remaining section 163(j) limitation, disallowed business interest expense carryforwards are deducted on a pro rata basis in the order of the taxable years in which they arose; and (iv) each member whose business interest expense is not fully absorbed by the group in the current taxable year carries the expense forward to the succeeding taxable year as a disallowed business interest expense carryforward.

Commenters posed several questions and comments with regard to these proposed rules. One commenter expressed concern that these provisions would create noneconomic and distortive allocations of disallowed business interest expense within consolidated groups. For example, assume P (the parent of a consolidated group) acts as a group's sole external borrower, and P on-lends the loan proceeds to S (a member of P's consolidated group) for use in S's business operations. Under the proposed regulations, any disallowed business interest expense would be allocated to P even though S is the economic user of the borrowed funds and may generate the income that supports the external debt. The commenter also expressed concern that, under the proposed regulations, consolidated groups effectively may decide which member will carry forward disallowed business interest expense by having that member borrow funds from third parties, regardless of whether that member actually uses the funds. The commenter raised similar concerns about business interest income, noting that a group may choose which member will loan funds outside the group and thereby affect which member's business interest expense is absorbed within the group.

To address the foregoing concerns, the commenter suggested that the final regulations (i) take intercompany interest income and expense into account for purposes of section 163(j), (ii) allocate current-year disallowed business interest expense to members without regard to whether the interest expense results from intercompany obligations or external borrowings, and (iii) de-link disallowed business interest expenses from intercompany interest income for purposes of the rules under § 1.1502–13. However, the commenter acknowledged that this approach could introduce unwarranted complexity. Alternatively, the commenter suggested that taxpayers be permitted to apply any reasonable approach (apart from tracing) consistent with the economics, subject to a narrowly tailored anti-avoidance rule.

In the proposed regulations, the Treasury Department and the IRS determined that intercompany obligations should be disregarded for purposes of section 163(j) for several reasons. First, section 163(j) is concerned with interest expense paid to external lenders, not internal borrowing between divisions of a single corporation (or between members of a consolidated group). In this regard, the Treasury Department and the IRS note that treating a member with intercompany debt but no external debt as having business interest expense could lead to strange results.

Second, the approach taken in the proposed regulations results in application of the section 163(j) limitation at the consolidated group level, consistent with the expressed intent of Congress (see H. Rept. 115–466, at 386 (2017)).

Third, such an approach is simpler for taxpayers to administer than an approach that would require consolidated groups to track disallowed business interest expense with regard to intercompany obligations across taxable years, as further discussed in the following paragraph. Allowing taxpayers to apply any reasonable approach (and to ignore or take into account interest expense on intercompany obligations as they determine to be appropriate) also would further complicate rather than simplify tax administration, particularly with regard to the application of section 163(j) to consolidated groups.

Fourth, as the commenter acknowledged, taking intercompany obligations into account for purposes of section 163(j) would complicate the application of § 1.1502–13. Section 1.1502–13 achieves single-entity treatment for a consolidated group by preventing intercompany transactions from creating, accelerating, avoiding, or deferring consolidated taxable income or liability. To this end, § 1.1502–13(c) ''matches'' the tax items of the members that are parties to an intercompany transaction. In the case of intercompany interest, income and deductions do not affect consolidated taxable income or liability because each side of the transaction ''nets out'' the other in each taxable year. If section 163(j) applied to intercompany payments of business interest expense, and if a consolidated group's section 163(j) limitation did not permit the deduction of all of the group's intercompany business interest expense, the interest income and expense would not net out each other. Thus, the group would need to separately track both the intercompany borrower's non-deductible expense and the intercompany lender's non-includible income through future taxable years.

The Treasury Department and the IRS acknowledge that disregarding intercompany obligations may lead to results in some circumstances that are less economically accurate than a regime that takes such obligations into account, but the Treasury Department and the IRS considered administrability as well as economic accuracy when promulgating the proposed regulations. Moreover, although disregarding intercompany obligations may grant consolidated groups the latitude to decide which member will incur business interest expense, consolidated groups also would have significant flexibility to allocate business interest expense within a group using intercompany obligations if such obligations were regarded for purposes of section 163(j).

Although the proposed rules in the Concurrent NPRM concerning CFC group elections do regard inter-CFC group net interest expense in allocating CFC group disallowed business interest expense, the CFC group setting is materially different from that of a consolidated group. First, in the context of a CFC group, neither § 1.1502–13 nor similar rules apply. Second, the location of disallowed business interest expense may have more effect on tax liability. In particular, disallowed business interest expense may affect the calculation of foreign tax credits and the amount of qualified business asset investment within the meaning of section 951A(d)(1) (QBAI) taken into account in determining a U.S. shareholder's tax liability under section 951A. This effect depends entirely on the particular CFC group member affected by disallowed business interest expense. Although the location of disallowed business interest expense has an effect on consolidated groups, this effect often will be less than in the CFC group context.

For the foregoing reasons, the final regulations do not apply section 163(j) to business interest expense or business interest income incurred on intercompany obligations, with one limited exception related to repurchase premium on obligations that are deemed satisfied and reissued, which is described in part V(C) of this Summary of Comments and Explanation of Revisions section.

Commenters also expressed concern that consolidated groups may have difficulty determining which member is the borrower on external debt if other group members are co-obligors or guarantors on the debt, and that, as a result, each member may have difficulty calculating its business interest expense for each taxable year. Commenters voiced similar concerns about the lack of parameters for determining the appropriate location of business interest income and floor plan financing interest expense within the group.

The Treasury Department and the IRS do not find this comment persuasive. Consolidated groups (and other related parties) are required to determine which member is entitled to a deduction for interest expense. Specifically, a consolidated group must use this information for purposes of computing consolidated taxable income under §§ 1.1502–11 and 1.1502–12 and making stock basis adjustments in members under § 1.1502–32. Moreover, consolidated groups must determine which member has incurred business interest expense for purposes of applying section 382 and the separate return limitation year (SRLY) rules. Consolidated groups must look to existing law to determine which member should be treated as incurring business interest expense or business interest income for purposes of section 163(j).

C. Repurchase Premium on Obligations That Are Deemed Satisfied and Reissued

As discussed in part V(B) of this Summary of Comments and Explanation of Revisions section, interest expense on intercompany obligations generally is disregarded for purposes of section 163(j). Thus, commenters asked whether repurchase premium that is treated as interest with respect to intercompany obligations should be subject to the section 163(j) limitation. In general, if debt that is not an intercompany obligation becomes an intercompany obligation (for example, if a member of a consolidated group acquires another member's debt from a non-member), the debt is treated for all Federal income tax purposes, immediately after it becomes an intercompany obligation, as having been satisfied by the issuer for cash in an amount equal to the holder's basis in the note and as having been reissued as a new intercompany obligation for the same amount of cash. See § 1.1502–13(g)(5)(ii)(A). Additionally, if a debt instrument is repurchased by the issuer for a price in excess of its adjusted issue price (as defined in § 1.1275–1(b)), the excess (repurchase premium) generally is deductible as interest for the taxable year in which the repurchase occurs. See § 1.163–7(c).

For example, S is a member of P's consolidated group, and S has borrowed $100x from unrelated X. At a time when S's note has increased in value to $130x due to a decline in prevailing interest rates, P purchases the note from X for $130x. Under § 1.1502–13(g)(5)(ii), S's note is treated as satisfied for $130x immediately after it becomes an intercompany obligation. As a result of the deemed satisfaction of the note, P has no gain or loss, and S has $30x of repurchase premium that is deductible as interest. See § 1.1502–13(g)(7)(ii), *Example 10.* Similarly, if S were to repurchase its note from X for $130x, S would have $30x of repurchase premium that is deductible as interest.

If S were to repurchase its note from X at a premium, the interest (in the form of repurchase premium) paid on that note would be subject to the section 163(j) limitation. See § 1.163(j)–1(b)(22)(i)(H) (treating repurchase premium that is deductible under § 1.163–7(c) as interest for purposes of section 163(j)). If section 163(j) does not apply to repurchase premium paid by S to P after P purchases S's note from X, the P group would obtain a different (and better) result than if S were to repurchase its own note. The Treasury Department and the IRS have determined that achieving different results under section 163(j) depending on which member repurchases external debt would be inconsistent with treating a consolidated group as a single entity for purposes of section 163(j) and would undermine the purpose of § 1.1502–13. Thus, the final regulations provide that, for purposes of section 163(j), if any member of a consolidated group purchases a member's note from a third party at a premium, the repurchase premium that is deductible under § 1.163–7(c) is treated as interest expense for purposes of section 163(j), regardless of whether the repurchase premium is treated as paid on intercompany indebtedness.

D. Intercompany Transfers of Partnership Interests

1. Overview of Proposed § 1.163(j)–4(d)(4)

Proposed § 1.163(j)–4(d)(4) provides that the transfer of a partnership interest in an intercompany transaction that does not result in the termination of the partnership is treated as a disposition for purposes of section 163(j)(4)(B)(iii)(II), regardless of whether the transfer is one in which gain or loss is recognized. Thus, the transferor member's excess business interest expense is eliminated rather than transferred to the transferee member. Proposed § 1.163(j)–4(d)(4) further provides that neither the allocation of excess business interest expense to a member from a partnership (and the resulting decrease in basis in the partnership interest) nor the elimination of excess business interest expense of a member upon a disposition of the partnership interest (and the resulting increase in basis in the partnership interest) affects basis in the member's stock for purposes of § 1.1502–32(b)(3)(ii). Instead, investment adjustments are made under § 1.1502–32(b)(3)(i) when the excess business interest expense from the partnership is absorbed by the consolidated group. See § 1.1502–32(b).

2. Intercompany Transfers of Partnership Interests Treated as Dispositions; Single-Entity Treatment; Application of § 1.1502–13

Commenters posed various questions and comments about the treatment of intercompany transfers of partnership interests as dispositions for purposes of section 163(j). For example, commenters asked why, in applying section 163(j) to consolidated groups, the proposed regulations treat such transfers as dispositions, rather than simply disregard the transfers, given that the proposed regulations generally treat consolidated groups as a single entity and disregard intercompany transactions for purposes of section 163(j).

The proposed regulations provide that intercompany transfers of partnership interests are treated as dispositions for purposes of section 163(j) because each member's separate ownership of interests in a partnership generally is respected (otherwise, a partnership whose interests are wholly owned by members of a consolidated group would be treated as a disregarded entity), and because the term ''disposition'' in section 163(j)(4)(B)(iii)(II) has broad application (for example, it applies to nonrecognition transactions). Moreover, if an intercompany transfer of partnership interests were not treated as a disposition (and if, as a result, basis were not restored to the transferor member), the amount of the transferor member's gain or loss on the intercompany transfer would be incorrect. Special rules also would be needed to account for the transfer of excess business interest expense from one member to another in a manner consistent with the purposes of § 1.1502–13 and to comply with the directive of section 1502 to clearly reflect the income of each member of the group.

Several commenters also noted problems with the approach in proposed §§ 1.163(j)–4(d)(4) and 1.1502–13(c)(7)(ii)(R), *Example 18.* These commenters pointed out that the approach in the proposed regulations does not achieve single-entity treatment because one member's transfer of its partnership interest to another member causes the transferor's excess business interest expense to be eliminated; thus, an intercompany transaction may alter the amount of business interest expense that is absorbed by the group. One commenter suggested a different approach under which the transferee could claim deductions for excess business interest expense to the extent the transferee is allocated excess taxable income from the same partnership. However, the commenter acknowledged that this approach would require additional rules under § 1.1502–13.

Another commenter suggested that intercompany transfers in which the transferee is the successor to the transferor (for example, in transactions to which section 381(a) applies, or in which the transferee's basis in the partnership interest is determined by reference to the transferor's basis) should not be treated as dispositions for purposes of section 163(j)(4)(B)(iii)(II). However, this approach would not result in an increase in the transferor member's (S's) basis in its partnership interest immediately before the transfer; thus, this approach would be inconsistent with § 1.1502–13, which requires the clear reflection of income at the level of the consolidated group member. This approach also would be inconsistent with section 163(j)(4)(B)(iii)(II), which clearly treats ''a transaction in which gain is not recognized in whole or in part'' as a disposition for purposes of that section.

Still another commenter observed that the analysis in proposed § 1.1502–13(c)(7)(ii)(R), *Example 18,* does not work in certain other fact patterns. In proposed § 1.1502–13(c)(7)(ii)(R), *Example 18,* P wholly owns S and B, both of which are members of P's consolidated group. S and A (an unrelated third party) are equal partners in PS1, which allocates $50x of excess business interest expense to each partner in Year 2. At the end of Year 2, S sells its PS1 interest to B at a $50x loss (S's excess business interest expense is eliminated, and S's basis in its PS1 interest is increased by $50x immediately before the sale). In Year 3, PS1 allocates $25x of excess taxable income to B. At the end of Year 4, B sells its PS1 interest to Z (an unrelated third party) for a $10x gain. The example concludes that S takes into account $25x of its loss in Year 3 as an ordinary loss, which matches B's inclusion of $25x of ordinary income in Year 3. The remaining $25x of S's $50x capital loss is taken into account in Year 4. The commenter noted that, although the analysis in proposed § 1.1502–13(c)(7)(ii)(R), *Example 18,* works under the facts presented, it would not work if, for example, S were to sell the PS1 interest to B at a gain (because S's gain and B's income could not be offset).

The Treasury Department and the IRS acknowledge the concerns raised by these commenters. The Treasury Department and the IRS are continuing to study the proper treatment of intercompany transfers of partnership interests that do not result in the termination of the partnership (intercompany partnership interest transfers), including whether such transfers should be treated as dispositions for purposes of section 163(j)(4)(B)(iii)(II). The final regulations reserve on issues relating to intercompany partnership interest transfers, and the Treasury Department and the IRS welcome further comments on such issues.

3. Possible Approach to Intercompany Partnership Interest Transfers

The Treasury Department and the IRS are considering various possible approaches to intercompany partnership interest transfers. Under one possible approach, such a transfer would be treated as a disposition by S; thus, S's excess business interest expense would be eliminated (and its basis in its partnership interest would be increased accordingly immediately before the transfer), as would S's negative section 163(j) expense (within the meaning of § 1.163(j)–6(h)(1)). However, unlike the approach in proposed § 1.163(j)–4(d)(4), B would be treated as if B had been allocated excess business interest expense or negative section 163(j) interest expense from the partnership in an amount equal to the amount of S's excess business interest expense or negative section 163(j) expense, respectively, immediately before the transfer. B's basis in its partnership interest would be adjusted under section 163(j)(4)(B)(iii)(I) and § 1.163(j)–6(h) to reflect the deemed allocation of excess business interest expense from the partnership. Similar rules would apply to intercompany transfers of partnership interests in nonrecognition transactions.

The foregoing approach would attempt to approximate single-entity treatment while treating the intercompany transfer of a partnership interest as a disposition for purposes of section 163(j)(4)(B)(iii)(II). To ensure that B has the same amount of excess business interest expense, negative section 163(j) expense, and disallowed business interest expense carryforwards as if S and B were divisions of a single corporation, this approach also would include special basis rules. For example, if S transfers its partnership interest to B at a gain, the excess of B's basis in the partnership interest at any time after the transfer over S's basis in the partnership interest immediately before the transfer would not be available to convert negative section 163(j) expense into excess business interest expense in the hands of B or to prevent excess business interest expense from converting into negative section 163(j) expense in the hands of B. Additionally, if adjustments to B's basis in its partnership interest under section 163(j)(4)(B)(iii)(I) and § 1.163(j)–6(h) (upon the deemed allocation of excess business interest expense from the partnership) would exceed B's basis, B would be treated as having a suspended negative basis adjustment in the partnership interest (similar to an excess loss account within the meaning of § 1.1502–19(a)(2)(i)).

The Treasury Department and the IRS request comments on possible approaches to intercompany partnership interest transfers, including the approach outlined in this part V(D)(3) of this Summary of Comments and Explanation of Revisions section.

4. Offsetting Excess Business Interest Expense and Adjusted Taxable Income Within the Consolidated Group

A commenter also recommended that, if the section 163(j) regulations do not treat partnerships wholly owned by members of the same consolidated group as aggregates rather than as entities (see part V(A) of this Summary of Comments and Explanation of Revisions section), the rules applicable to such partnerships should be simplified. For example, the excess taxable income allocated to one member partner could be made available to offset excess business interest expense allocated to another member partner.

The commenter's recommendation presents several issues. For example, the commenter's recommendation would entail disregarding the location of excess business interest expense and excess taxable income within a consolidated group. Such an approach would not fully respect each member's separate interest in a partnership and would not clearly reflect the taxable income of the members of the group. See section 1502; see also part V(D)(2) of this Summary of Comments and Explanation of Revisions section. Further, to the extent the ownership structure of the group is altered by an intercompany transfer of the partnership interest, substantial additional rules under § 1.1502–13 would be required.

5. Intercompany Nonrecognition Transactions

In proposed §§ 1.163(j)–4(d)(4) and 1.1502–13(c)(7)(ii)(S), *Example 19,* the intercompany transfer of a partnership interest in a nonrecognition transaction is treated as a disposition for purposes of section 163(j)(4)(B)(iii)(II). In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments as to whether such transfers should constitute dispositions for purposes of section 163(j)(4)(B)(iii)(II) and, if so, how § 1.1502–13(c) should apply if there is excess taxable income in a succeeding taxable year. In such a case, S would have no intercompany item from the intercompany transfer, and B would take a carryover basis in the partnership interest (this amount would include any basis increase to reflect S's unused excess business interest expense under section 163(j)(4)(B)(iii)(II)).

One commenter agreed that, based on the plain language of section 163(j)(4)(B)(iii)(II), intercompany transfers that are nonrecognition transactions should be treated as dispositions. Another commenter stated that such transfers generally should not be treated as dispositions (if the transferee is the successor to the transferor, as previously discussed), but that, if such transfers are treated as dispositions, no redeterminations should be made under § 1.1502–13(c) with respect to S unless S recognizes gain in the intercompany transfer.

The Treasury Department and the IRS continue to study the proper treatment of intercompany partnership interest transfers and welcome further comments on this issue.

6. Basis Adjustments Under § 1.1502–32

A commenter stated that the approach to basis adjustments under § 1.1502–32 in the proposed regulations may lead to temporary inside/outside basis disparities. Although the commenter generally described this approach as reasonable and consistent with the application of both section 163(j) and § 1.1502–32, the commenter suggested that it may lead to anomalous results in certain cases. The commenter requested an example to illustrate the application of the matching and acceleration rules in the case of an intercompany transfer of an interest in a partnership with disallowed business interest expense.

When S (a member of a consolidated group that is not the common parent) is allocated excess business interest expense from a partnership, S's basis in the partnership is reduced under section 163(j)(4)(B)(iii)(I). Although S's basis in the partnership is reduced, S has excess business interest expense in the same amount, and S's overall inside attribute amount is unchanged. Because there is no net change to S's inside attribute amount, § 1.1502–32 does not apply to reduce other members' basis in S's stock, and there is no inside/outside disparity. Moreover, nothing in the final regulations affects the operation of § 1.1502–32(a), which generally requires adjustments to a member's basis in its S stock to reflect S's distributions and S's items of income, gain, deduction, and loss that are taken into account by the group while S is a member. Thus, the final regulations make no changes in response to this comment.

7. Partnership Terminations

In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments on the treatment of the transfer of a partnership interest in an intercompany transaction that results in the termination of the partnership. Some commenters recommended that the transfer be treated as a disposition for purposes of section 163(j)(4)(B)(iii)(II) and proposed § 1.163(j)–6(h)(3). Other commenters recommended that, under Revenue Ruling 99–6, 1999–1 C.B. 432, if the transferee member (B) also were a partner in the partnership before the intercompany transfer, B should be viewed as (i) receiving a distribution of assets from the terminating partnership with respect to its partnership interest, and (ii) purchasing the partnership's assets deemed distributed to the transferor member (S).

The Treasury Department and the IRS are continuing to study the proper treatment of intercompany transfers of partnership interests that result in the termination of the partnership. But see § 1.163(j)–6(h)(3) with respect to partnership terminations generally.

E. Application of § 1.1502–36 to Excess Business Interest Expense

Under proposed § 1.163(j)–4(d)(4), a partner's change in status as a member of a consolidated group is not treated as a disposition for purposes of section 163(j)(4)(B)(iii)(II) and proposed § 1.163(j)–6(h)(3). In other words, if a corporation becomes or ceases to be a member of a consolidated group, and if that corporation is a partner in a partnership, that corporation's entry into or departure from a consolidated group does not trigger basis adjustments under section 163(j)(4)(B)(iii)(II). However, in the preamble to the proposed regulations, the Treasury Department and the IRS requested comments as to whether additional rules are needed to prevent loss duplication upon the disposition of stock of a subsidiary member (S) holding partnership interests.

Section 1.1502–36 contains the unified loss rule, which limits the ability of a consolidated group to recognize non-economic or duplicated losses on the transfer of S stock. The rule applies when a group member transfers a loss share of S stock. If § 1.1502–36(d) applies to the transfer of a loss share, the attributes of S and its lower-tier subsidiaries generally are reduced as needed to prevent the duplication of any loss recognized on the transferred stock. Such attributes include capital loss carryovers, NOL carryovers, deferred deductions, and basis in assets other than cash and general deposit accounts. See § 1.1502–36(d)(4).

As noted in the preamble to the proposed regulations, the Treasury Department and the IRS have determined that disallowed business interest expenses should be treated as deferred deductions for purposes of § 1.1502–36 (see proposed § 1.1502–36(f)(2)). A commenter recommended that excess business interest expense also be treated as a deferred deduction in determining the net inside attribute amount for purposes of § 1.1502–36(c) and (d). Additionally, the commenter recommended that a consolidated group be permitted to elect to reattribute excess business interest expense from S to the common parent under § 1.1502–36(d)(6) if the common parent also is a partner in the partnership that allocated excess business interest expense to S.

The Treasury Department and the IRS agree that excess business interest expense should be treated as an attribute that is taken into account in determining the net inside attribute amount for purposes of § 1.1502–36(c) and (d). However, the Treasury Department and the IRS have determined that excess business interest expense is more akin to basis (a Category D attribute) than to deferred deductions (a Category C attribute) (see § 1.1502–36(d)(4)(i)). Section 1.163(j)–4(e)(4) reflects this conclusion.

The Treasury Department and the IRS also have determined that excess business interest expense should not be eligible for reattribution under § 1.1502–36(d)(6) because the election is not available with respect to Category D attributes. Thus, the final regulations do not adopt this recommendation.

F. Calculating ATI for Cooperatives

Proposed § 1.163(j)–1(b)(1) defines ATI as the taxable income of the taxpayer for the taxable year, with certain adjustments. Proposed § 1.163(j)–4(b)(4) provides a special rule for calculating the ATI of a RIC or REIT, allowing the RIC or REIT not to reduce its taxable income by the amount of any deduction for dividends paid. The preamble to the proposed regulations also requested comments on whether additional special rules are needed for specific types of taxpayers, including cooperatives.

A commenter asked that the final regulations include a special rule for calculating the ATI of cooperatives subject to taxation under subchapter T of the Code. Under this special rule, taxable income would not be reduced by amounts deducted under section

1382(b)(1) (patronage dividends), section 1382(b)(2) (amounts paid in redemption of nonqualified written notices of allocation distributed as patronage dividends), or section 1382(c) (certain amounts incurred by farm cooperatives described in sections 521 and 1381(a)(1)). The commenter reasoned that such amounts are earnings passed on to members and are therefore analogous to dividends paid by a RIC or REIT to its investor.

The Treasury Department and the IRS agree that, for purposes of section 163(j), amounts deducted by cooperatives under sections 1382(b)(1), (b)(2), and (c) are similar to amounts deducted by RICs and REITs for dividends paid to their investors. The final regulations adopt a rule providing that, for purposes of calculating ATI, the tentative taxable income of a cooperative subject to taxation under sections 1381 through 1388 is not reduced by such amounts. In order to provide similar treatment to similarly situated taxpayers, the final regulations also provide that, for purposes of calculating ATI, the tentative taxable income of cooperatives not subject to taxation under subchapter T of the Code is not reduced by the amount of deductions equivalent to the amounts deducted by cooperatives under sections 1382(b)(1), (b)(2), and (c).

G. Calculating ATI for a Consolidated Group

Proposed § 1.163(j)–1(b)(1) defines ATI as the taxable income of the taxpayer for the taxable year, with certain adjustments. For example, ATI is computed without regard to the amount of any NOL deduction under section 172. See proposed § 1.163(j)–1(b)(1)(i)(B).

As noted in part V(B) of this Summary of Comments and Explanation of Revisions section, for purposes of calculating the ATI of a consolidated group, the relevant taxable income is the group's consolidated taxable income, determined under § 1.1502–11 without regard to any carryforwards or disallowances under section 163(j). See proposed § 1.163(j)–4(d)(2)(iv). Commenters asked for clarification that a consolidated group's ATI does not take into account any NOL deductions available under section 172 and § 1.1502–11(a)(2) that result from either the carryback or carryforward of NOLs.

Proposed § 1.163(j)–4(d)(2)(iv) does not expressly mention the adjustments made to ATI in proposed § 1.163(j)–1(b)(1) because those adjustments are generally applicable (for example, the adjustment for NOLs applies to all taxpayers to whom section 172 applies, regardless of whether such taxpayers file a consolidated return). Moreover, there is no exception in proposed § 1.163(j)–4(d)(2)(iv) to the adjustment for NOLs in proposed § 1.163(j)–1(b)(1)(i)(B). Thus, under these provisions, a consolidated group's ATI would not take into account any NOL deductions resulting from the carryback or carryforward of NOLs. The Treasury Department and the IRS have determined that no change to proposed § 1.163(j)–4(d)(2)(iv) is needed to effectuate this result.

H. Application of Section 163(j) to Life-Nonlife Groups

Proposed § 1.163(j)–4(d)(2) provides that a consolidated group has a single section 163(j) limitation and that, for purposes of calculating the group's ATI, the relevant taxable income is the group's consolidated taxable income. However, § 1.1502–47 requires consolidated groups whose members include life insurance companies and other companies (life-nonlife groups) to adopt a subgroup method to determine consolidated taxable income. (One subgroup is the group's nonlife companies; the other subgroup is the group's life insurance companies.) Under the subgroup method, each subgroup initially computes its own consolidated taxable income, and there are limitations on a life-nonlife group's ability to offset one subgroup's income with the other subgroup's loss.

In light of the apparent tension between proposed § 1.163(j)–4(d)(2) and the subgroup method in § 1.1502–47, one commenter asked for clarification that there are not separate section 163(j) limitations for each subgroup in a life-nonlife group.

The subject matter of this comment is beyond the scope of the final regulations. The Treasury Department and the IRS expect to issue future guidance regarding the interaction of section 163(j) and § 1.1502–47 and welcome further comments on this topic.

I. Application of Section 163(j) to Tax-Exempt Entities

Proposed § 1.163(j)–1(b)(36) defines a tax-exempt corporation but does not define other types of tax-exempt organizations. Thus, a commenter asked for clarification as to whether section 163(j) applies solely to tax-exempt corporations or whether it also applies to other entities subject to tax under section 511. The final regulations clarify that section 163(j) applies to all entities that are subject to tax under section 511.

The commenter also suggested that section 163(j) should not apply to state colleges and universities described in section 511(a)(2)(B). The Treasury Department and the IRS have found nothing in the statute or legislative history to suggest that Congress intended special treatment for state colleges and universities to the extent such organizations are subject to tax under section 511. Therefore, the final regulations do not adopt this recommendation.

J. Partnership Investment Income and Corporate Partners

Under the proposed regulations, a partnership's investment interest income and investment expense are allocated to each partner in accordance with section 704(b), and the effect of the allocation is determined at the partner level. In general, any investment interest, investment income, and investment expense allocated by a partnership to a C corporation partner is treated by the partner as allocable to a non-excepted trade or business of the partner for purposes of section 163(j). See proposed §§ 1.163(j)–4(b)(3)(i) and 1.163(j)–10(b)(6).

In light of the statutory restriction against including investment income in a partner's ATI (see section 163(j)(8)(A)(i)), a commenter requested confirmation that a partnership's investment income is treated as properly allocable to a trade or business of (and thus is included in the ATI of) a corporate partner, perhaps by adding an example to illustrate the application of this rule.

Proposed § 1.163(j)–10(b)(6) provides that any investment income or investment expenses that a partnership receives, pays, or accrues and that is treated as properly allocable to a trade or business of a C corporation partner under proposed § 1.163(j)–4(b)(3)(i) is treated as properly allocable to a non-excepted trade or business of the C corporation partner. Thus, if a partnership incurs investment interest expense, any portion of that expense that is allocable to a C corporation partner is treated as a business interest expense of that partner that is subject to the section 163(j) limitation. However, if the partnership also has investment interest income, any portion thereof that is allocable to a C corporation partner is treated as business interest income of the partner, and any other investment income of the partnership that is allocable to the C corporation partner increases the partner's ATI. See § 1.163(j)–4(b)(7)(ii), *Example 2.*

To the extent that an investment item or other item of a partnership is with respect to property for which an election has been made by the partnership to treat as an electing real property trade or business or electing farming business, such item is treated as properly allocable to an excepted trade or business. This rule is necessary because the final regulations permit elections for some assets and activities to be an excepted trade or business even when such assets and activities are not trades or businesses for section 162 purposes. See part X(A) of this Summary of Comments and Explanation of Revisions section.

The final regulations also expand proposed § 1.163(j)–4(b)(3)(i) to cover not only a partnership's items of investment interest, investment income, and investment expense, but also a partnership's other separately stated tax items that are subject to neither section 163(j) nor section 163(d). Such items might include tax items allocable to rental activities that do not rise to the level of a section 162 trade or business that otherwise give rise to allowable deductions (such as under section 212 as it existed under prior law) that are subject to section 469. Thus, such items are treated as properly allocable to a trade or business of a C corporation partner as well.

K. Earnings and Profits of a Corporate Partner

Proposed § 1.163(j)–4(c)(1) generally provides that the disallowance and carryforward of a deduction for a C corporation's business interest expense under proposed § 1.163(j)–2 does not affect whether or when the business interest expense reduces the corporation's earnings and profits. Some commenters suggested that, if the business interest expense in question is incurred by a partnership rather than by the C corporation partner, the partner should reduce its earnings and profits twice with respect to that expense—once when the expense is allocated from the partnership to the partner, and again when the partner claims a deduction with respect to that expense (after the excess business interest expense allocated to that partner is treated as business interest expense and deducted by that partner).

The Treasury Department and the IRS have determined that the proposed regulations do not permit a C corporation partner to reduce its earnings and profits twice with respect to business interest expense incurred by a partnership. The final regulations are modified to clarify this point.

Proposed § 1.163(j)–4(c)(3) also provides a special earnings and profits rule for C corporations (other than REITs or RICs) with respect to excess business interest expense allocated from a partnership. Under this rule, the C corporation partner must increase its earnings and profits upon the disposition of the partnership interest to reflect the amount of excess business interest expense that the partner did not take into account while it held the partnership interest. The Treasury Department and the IRS have determined that the same rule should apply with respect to negative section 163(j) expense, and the final regulations have been modified accordingly.

VI. Comments on and Changes to Proposed § 1.163(j)–5: General Rules Governing Disallowed Business Interest Expense Carryforwards for C Corporations

Section 1.163(j)–5 provides rules regarding disallowed business interest expense carryforwards for taxpayers that are C corporations, including members of a consolidated group. The following discussion addresses comments relating to proposed § 1.163(j)–5.

A. Absorption of Disallowed Business Interest Expense Carryforwards Before Use of NOLs in Life-Nonlife Groups

Proposed § 1.163(j)–5(b)(3) provides rules regarding the treatment of disallowed business interest expense carryforwards of a consolidated group. Commenters asked for confirmation that, in the context of a life-nonlife group, such carryforwards are factored into taxable income at the subgroup level before NOLs are carried forward and limited under section 1503(c)(1).

In general, a consolidated group must determine the amount of business interest expense (whether current-year or carryforwards) that can be absorbed in a particular taxable year before determining whether NOLs can be carried forward or back to that taxable year. However, the specific subject matter of this comment is beyond the scope of the final regulations. The Treasury Department and the IRS expect to issue future guidance regarding the interaction of section 163(j) and § 1.1502–47 and welcome further comments in this regard.

B. Carryforwards From Separate Return Limitation Years

Proposed § 1.163(j)–5(d) contains rules for consolidated groups regarding disallowed business interest expense carryforwards from a separate return limitation year (a SRLY; see § 1.1502–1(f)). Under these rules, the disallowed business interest expense carryforwards of a member arising in a SRLY that are included in a group's business interest expense deduction for any taxable year may not exceed the group's section 163(j) limitation for that year, determined by reference only to the member's tax items for that year (the section 163(j) SRLY limitation). See proposed § 1.163(j)–5(d)(1). Additionally, disallowed business interest expense carryforwards of a member arising in a SRLY would be available for deduction by the consolidated group in the current year only to the extent the group had remaining section 163(j) limitation after deducting current-year business interest expense and disallowed business interest expense carryforwards from earlier taxable years, and only to the extent the section 163(j) SRLY limitation for the current year exceeded the amount of the member's business interest expense already deducted by the group in that year. In addition, SRLY-limited disallowed business interest expense carryforwards must be deducted on a pro rata basis with non-SRLY limited disallowed business interest expense carryforwards from taxable years ending on the same date. See proposed § 1.163(j)–5(d)(2).

Commenters asked several questions about the SRLY rules in proposed § 1.163(j)–5(d). In particular, commenters asked why the section 163(j) SRLY limitation is calculated annually rather than on an aggregate or cumulative basis, as is the case for NOLs. (Section 1.1502–21(c)(1)(i) generally limits the amount of a member's NOL carryforwards and carrybacks from a SRLY that may be included in the group's consolidated net operating loss deduction to the member's aggregate contribution to the group's consolidated taxable income for the entire period the member has been a group member, not just for the taxable year in question). More specifically, a commenter noted that the SRLY rules in § 1.1502–21(c) were designed to produce a result that roughly approximates the absorption that would have occurred if the SRLY member had not joined a consolidated group. In contrast, the annual section 163(j) limitation in proposed § 1.163(j)–5(d) could put the SRLY member in a worse position than if such member had not joined a consolidated group.

For example, if S were a standalone corporation with $100x of disallowed business interest expense carryforwards at the start of Year 2, and if S's section 163(j) limitation were $30 in Year 2, S could deduct $30x of its carryforwards. In comparison, if S joined a consolidated group at the start of Year 2, and if the group's section 163(j) limitation were $0 in Year 2, S could not deduct any of its $100x of carryforwards in Year 2 even if S's standalone section 163(j) limitation were $30x in that year. This result is correct for the P group for Year 2 given Congress's intent that the section 163(j) limitation apply at the consolidated group level. However, under the annual measurement approach in the proposed regulations, S also could not deduct any of its carryforwards in Year 3 if S had a standalone section 163(j) limitation of $0 in that year, even if the group's section 163(j) limitation were positive in that year. Thus, S would be in a worse position (with respect to the deduction of its disallowed business interest expense carryforwards) than if S had not joined a consolidated group.

To put S in roughly the same position as if S were a standalone corporation, commenters recommended the creation of a cumulative section 163(j) register under which the amount of a member's SRLY carryforwards that may be absorbed by the consolidated group in a taxable year may not exceed (i) the member's contributions (positive and negative) to the group's section 163(j) limitation in all consolidated return years, less (ii) the member's business interest expense (including carryforwards) absorbed by the group in all consolidated return years. For these purposes, and unlike the general rule in section 163(j)(1) and proposed § 1.163(j)–2(b)(2), the adjustment to a member's cumulative section 163(j) SRLY register for any taxable year or its total register for any taxable year could be less than zero.

In the preamble to the proposed regulations, the Treasury Department and the IRS stated that applying an aggregate or cumulative approach to the section 163(j) SRLY limitation would be inconsistent with congressional intent because Congress did not retain the excess limitation carryforward provisions from old section 163(j). One commenter expressed agreement with this conclusion. However, other commenters noted that applying a cumulative section 163(j) SRLY register would not effectuate the carryforward of excess limitation at the level of the consolidated group. In other words, although the SRLY member would be able to deduct its SRLY disallowed business interest expense carryforwards in a taxable year to the extent of that member's cumulative (rather than annual) contribution to the group's section 163(j) limitation, the SRLY member's ability to deduct such carryforwards still would be subject to the group's annual section 163(j) limitation.

After considering the comments received, the Treasury Department and the IRS have determined that a cumulative section 163(j) SRLY register would better approximate the results under section 163(j) if the SRLY member had not joined a consolidated group, and that this approach is not inconsistent with congressional intent. Therefore, the final regulations adopt a cumulative section 163(j) SRLY register.

The cumulative section 163(j) SRLY register operates in a manner similar to, but is separate and distinct from, the cumulative register for NOLs described in § 1.1502–21(c). In computing a member's section 163(j) SRLY register, the intercompany transaction rules of § 1.1502–13 generally continue to apply; thus, for example, intercompany income items and intercompany deductions and losses (to the extent absorbed by the group) generally are taken into account in computing the section 163(j) SRLY register. However, interest income and expense from intercompany obligations are not taken into account in computing the section 163(j) SRLY register. This approach approximates the SRLY member's capacity to utilize carryforwards on a standalone basis while harmonizing with the single-entity application of section 163(j) to consolidated groups. Under this approach, intercompany interest income and expense items will neither increase nor decrease the SRLY register.

In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments on another alternative to both an annual register and a cumulative register—removing the SRLY limitation from a member's SRLY-limited disallowed business interest expense carryforwards, to the extent of the member's standalone section 163(j) limitation, in taxable years in which the member's standalone section 163(j) limitation exceeds the consolidated group's section 163(j) limitation. A commenter endorsed this approach. However, other commenters expressed concern that this approach would be more distortive than a cumulative register approach. The Treasury Department and the IRS agree that a cumulative register more closely approximates the results on a standalone basis than this alternative approach. Thus, the final regulations adopt a cumulative register approach rather than this alternative approach.

Commenters also expressed concern that proposed § 1.163(j)–5(d)(2) would treat SRLY carryforwards as available for deduction only to the extent the amount of the SRLY member's business interest expense already deducted by the group in the current year does not exceed the member's annual section 163(j) SRLY limitation. The adoption of the cumulative section 163(j) SRLY limitation mechanism, with the associated reduction to reflect all business interest expense of that member that is absorbed by the group, obviates the issues highlighted in the comment. The final regulations retain the other SRLY limitations in proposed § 1.163(j)–5(d)(2).

C. Offsetting Business Interest Expense With Business Interest Income and Floor Plan Financing Interest Expense at the Member Level

As described in part V(B) of this Summary of Comments and Explanation of Revisions section, proposed § 1.163(j)–5(b)(3) provides, in part, that if the aggregate amount of members' business interest expense (including carryforwards) exceeds the consolidated group's section 163(j) limitation for the current year, then each member with current-year business interest expense and current-year business interest income or floor plan financing interest expense deducts current-year business interest expense to the extent of its current-year business interest income and floor plan financing interest expense. Thereafter, if the group has any remaining section 163(j) limitation, each member with remaining current-year business interest expense deducts a pro rata portion thereof.

A commenter stated that offsetting business interest expense with business interest income or floor plan financing interest expense at the member level seems inconsistent with the single-entity principles adopted by the proposed regulations. Moreover, the commenter expressed concern that a consolidated group could choose where to incur business interest income within a group and thereby affect which member has disallowed business interest expense carryforwards. In addition, the commenter asserted that a group may have difficulty determining which member has incurred business interest income and floor plan financing interest expense (see the discussion in part V(B) of this Summary of Comments and Explanation of Revisions section). Thus, the commenter recommended an alternative approach that does not require such offsetting at the member level.

The Treasury Department and the IRS acknowledge that netting business interest income and floor plan financing interest expense against business interest expense at the member level deviates from a ''pure'' single-entity approach. This approach was adopted in the proposed regulations to give effect to section 163(j)(1) (which allows taxpayers to deduct business interest expense to the full extent of business interest income and floor plan financing interest expense) and to ensure that income tax liability is clearly reflected at the member level in accordance with section 1502 and § 1.1502–13. Further, because consolidated groups are under common control by definition (see section 1504), a consolidated group largely has control over the location of interest expense, even before the application of section 163(j). With regard to the comment regarding the difficulty of determining which member actually has incurred an interest expense, section 61 provides that interest income is includible in gross income, and section 163 provides rules by which interest expense is deductible in computing the taxable income. Section 1.1502–12 also requires consolidated group members to report interest income and expense at the member level for purposes of computing separate taxable income. Thus, the final regulations do not adopt the commenter's recommendation.

VII. Comments on and Changes to Section 1.163(j)–6: Application of the Business Interest Expense Deduction Limitations to Partnerships and Subchapter S Corporations

As discussed in the preamble to the proposed regulations, § 1.163(j)–6 provides general rules regarding the application of section 163(j)(4) to partnerships, S corporations, and their owners, including rules on how to calculate the limitation and how to treat disallowed business interest expense carryforwards. The following discussion addresses comments relating to proposed § 1.163(j)–6.

A. Partnership-Level Calculation and Allocation of Section 163(j) Excess Items

1. Nonseparately Stated Taxable Income or Loss of the Partnership

Section 163(j)(4)(A)(ii)(II) states that a partner's excess taxable income is determined in the same manner as the nonseparately stated taxable income or loss of the partnership. Section 163(j)(4)(B)(i)(II) states that excess business interest expense is allocated to each partner in the same manner as the non-separately stated taxable income or loss of the partnership. Similarly, excess business interest income is allocated to each partner in the same manner as the nonseparately stated taxable income or loss of the partnership.

As highlighted in the proposed regulations, the phrase ''nonseparately stated taxable income or loss of the partnership'' is not defined in section 163(j), and it has not previously been defined by statute or regulations.[1] The phrase ''in the same manner as'' is also undefined. The proposed regulations interpreted the phrase ''nonseparately stated taxable income or loss,'' as it is used in sections 163(j)(4)(A)(ii)(II) and 163(j)(4)(B)(i)(II), as meaning the items comprising adjusted taxable income, business interest income, and business interest expense of the partnership. The legislative history and structure of the statute suggest the purpose of the phrase ''nonseparately stated taxable income or loss of the partnership'' is to help coordinate the section 163(j) limit imposed at the partnership and partner levels.

Section 163(j)(4)(A)(i) uses this phrase when describing business interest expense that already has been tested at the partnership level. In general, an item included in nonseparately stated taxable income or loss of a partnership under section 702(a)(8) loses its tax character in the hands of the partner to whom it is allocated. By providing that such business interest expense is treated as a nonseparately stated item, section 163(j)(4)(A)(i) causes such business interest expense to lose its character as business interest expense, thus preventing it from being subject to retesting at the partner level under section 163(j). Although it does not use the same phrase, section 163(j)(4)(A)(ii)(I), in conjunction with section 163(j)(4)(C), similarly provides that, to the extent the partnership's adjusted taxable income was used in its section 163(j) calculation, such adjusted taxable income is not included in a partner's section 163(j) calculation. Consistent with this principle, proposed § 1.163(j)–6(e)(4) provided similar rules to prevent the double counting of business interest income. Therefore, interpreting the phrase ''nonseparately stated taxable income or loss of the partnership,'' as it is used in section 163(j)(4) as meaning the items comprising adjusted taxable income, business interest income, and business interest expense of the partnership (hereinafter, ''section 163(j) items'') is supported by the statute, which requires each of these items to be taken into account at the partnership level and prohibits the double counting of such items in the partner's section 163(j) calculation.

To allocate excess taxable income, excess business interest income, and excess business interest expense (hereinafter, ''section 163(j) excess items'') ''in the same manner'' as the ''nonseparately stated taxable income or loss of the partnership'' (that is, the section 163(j) items), proposed § 1.163(j)–6(f)(2) provided an 11-step calculation that, when completed by the partnership, provides the partnership with an allocation of each of its section 163(j) excess items to each of its partners. This resulting array of allocations is consistent with the Treasury Department and the IRS's resolution of the three descriptive (1 through 3) and two normative (4 through 5) issues outlined in part 6(D)(1) of the Explanation of Provisions section in the proposed regulations: (1) Section 163(j) is applied at the partnership level; (2) a partnership cannot have both excess taxable income (or excess business interest income) and excess business interest expense in the same taxable year; (3) parity must be preserved between a partnership's deductible business interest expense and section 163(j) excess items and the aggregate of each partner's share of deductible business interest expense and section 163(j) excess items from such partnership; (4) if, in a given year, a partnership has both deductible business interest expense and excess business interest expense, a partnership should not allocate excess business interest expense to a partner to the extent such partner was allocated the items comprising ATI (or business interest income) that supported the partnership's deductible business interest expense; and (5) if, in a given year, a partnership has excess taxable income (or excess business interest income), only partners allocated more items comprising ATI (or business interest income) than necessary to support their allocation of business interest expense should be allocated a share of excess taxable income (or excess business interest income).

In general, the 11-step calculation preserves the entity-level calculation required in section 163(j)(4) while also preserving the economics of the partnership, including respecting any special allocations made in accordance with section 704 and the regulations under section 704 of the Code. Stated otherwise, the allocations of section 163(j) excess items prescribed by the 11-step calculation attempt to reflect the aggregate nature of partnerships under subchapter K of the Code while remaining consistent with the application of section 163(j) at the partnership level.

The Treasury Department and the IRS requested comments on the 11-step calculation in the preamble to the

[1] Sections 163(j)(4)(A)(i) and (B)(i)(II) use the word ''nonseparately'' (no hyphen), but section 163(j)(4)(A)(ii)(II) uses the word ''non-separately'' (hyphen). For purposes of consistency, these final regulations use ''nonseparately'' when discussing the phrase at issue.

proposed regulations. Specifically, the Treasury Department and the IRS requested comments regarding alternative methods for allocating deductible business interest expense and section 163(j) excess items in a manner that permits partners that bear the taxable income supporting the deductible business interest expense to be allocated a disproportionate share of deductible business interest expense and excess taxable income.

2. Requested Clarifications and Modifications

Commenters requested several clarifications of and modifications to the 11-step calculation. First, commenters requested confirmation that a partnership's allocations of section 163(j) excess items pursuant to the 11-step calculation will be considered to meet the requirements of section 704(b). The final regulations confirm that allocations pursuant to the 11-step calculation meet the requirements of section 704(b). Nothing in the 11-step calculation prohibits a partnership from making an allocation to a partner of any section 163(j) item that is otherwise permitted under section 704 and the regulations thereunder. Accordingly, any calculations in the 11-step calculation are solely for the purpose of determining each partner's section 163(j) excess items, and do not otherwise affect any other provision under the Code, such as section 704(b). Further, the statement in the proposed regulations that the 11-step calculation is solely for section 163(j) purposes and does not apply for any other purposes of the Code does not mean that section 163(j) excess items have no effect on either outside basis or capital accounts. To illustrate this point, § 1.163(j)–6(o)(17), *Example 17* has been revised to show the beginning and ending outside basis and capital accounts after applying the 11-step calculation.

To further clarify that the allocation of section 163(j) excess items pursuant to the 11-step calculation will be sustained under section 704, a special rule has been added to § 1.704–1(b)(4). The allocation of deductible and nondeductible business interest expense does not have economic effect because classifying a portion of the interest expense as nondeductible merely changes the tax character of the item. Accordingly, § 1.704–1(b)(4)(xi) is added to clarify that, if § 1.163(j)–6(f) is satisfied, the allocation of section 163(j) excess items will be deemed to be in accordance with the partners' interests in the partnership.

Second, commenters recommended the 11-step calculation take remedial allocations into account. Commenters noted that the exclusion of remedial allocations from the partnership-level computation could frustrate the ability of the 11-step calculation to reach the most equitable result given its purpose. The Treasury Department and the IRS acknowledge that taking remedial allocations into account in the 11-step calculation after 2021 might produce an equitable result. However, because remedial income would not always be offset by remedial losses prior to 2022 for purposes of computing ATI, the Treasury Department and that IRS have determined that taking remedial allocations into account in the 11-step calculation would not achieve appropriate results in all circumstances. Therefore, the Treasury Department and the IRS decline to accept the recommendation.

Third, a commenter recommended that the final regulations allow partnerships to make remedial allocations of excess taxable income. Under this recommended modification to the 11-step calculation, if a partner receives an allocation of taxable income in excess of such partner's allocation of excess taxable income, the partnership could elect to create positive remedial excess taxable income in the amount of the excess and allocate such positive remedial excess taxable income to the affected partner. The partnership also would create an offsetting negative remedial excess taxable income item in an equal amount that would be allocated to the other partners. The Treasury Department and the IRS do not adopt this recommendation in the final regulations in light of the fact that the definition of ''excess taxable income'' is statutory and the statute does not appear to contemplate negative excess taxable income.

3. Recommended Alternative Methods

Commenters recommended the final regulations retain the 11-step calculation. Additionally, commenters recommended that the final regulations provide alternative methods for allocating section 163(j) excess items in addition to the 11-step calculation. The commenters seeking an alternative method expressed concern about the complexity of the 11-step calculation—specifically, that the required computations and recordkeeping are excessive for many taxpayers. Commenters argued that the attempted precision of the 11-step calculation should be weighed against its complexity and compared to the reduced precision that could be achieved through simpler methods.

As an alternative to the 11-step calculation, commenters recommended the final regulations allow taxpayers to adopt any reasonable method for allocating section 163(j) excess items, provided the method does not produce results inconsistent with the Treasury Department and the IRS's resolution of the five issues articulated in the preamble to the proposed regulations. See part VII(A)(1) of this Summary of Comments and Explanation of Revisions section. Commenters provided multiple examples of reasonable methods, and they recommended that the final regulations treat section 163(j) excess item allocations as reasonable if the allocations are: (1) Reasonably consistent with the allocations of the corresponding items under section 704(b); (2) in proportion to the allocation of the underlying section 163(j) item; (3) in proportion to the manner in which the partners bear liability for the debt or, in the case of non-recourse debt, in proportion to the manner in which profits will be allocated in order to repay the debt; or (4) the result of arms-length bargaining among partners with adverse tax interests.

The Treasury Department and the IRS do not adopt any of these alternatives in the final regulations. Each of the alternatives recommended by commenters requires an application of section 163(j) at the partnership level, a determination of each partner's share of the partnership's section 163(j) items, and a final determination of each partner's section 163(j) excess items that takes into account each partner's share of the partnership's section 163(j) items. These three determinations mirror steps 1, 2, and 11 (respectively) of the 11-step calculation. The Treasury Department and the IRS recognize the complexity of the computations and recordkeeping imposed by the statute on partnerships, but the Treasury Department and the IRS have concluded that the computations and recordkeeping associated with steps 1, 2, and 11 of the 11-step calculation are unavoidable under any approach. As such, the commenters' recommendation is, in effect, that the final regulations allow alternatives to steps 3 through 10 of the 11-step calculation.

With respect to steps 3 through 10, the Treasury Department and the IRS agree that these computations add to the complexity already required by the statute; thus, a worksheet and multiple examples have been provided to aid in the completion of these computations. However, the Treasury Department and the IRS have concluded that these computations are not overly burdensome given that the partnerships required to perform these calculations already are experienced with handling the complexities associated with special allocations or section 704(c) allocations. In terms of recordkeeping, taxpayers are not required to keep records of steps 3 through 10 because compliance with the 11-step calculation can be determined solely based on the records associated with steps 1, 2, and 11. Moreover, in terms of accuracy, the alternatives fall short of achieving the purpose of steps 3 through 10, which is to align deductible business interest expense with the ATI and business interest income that supported such deduction at the partnership level.

For example, consider the recommended alternative of allocating section 163(j) excess items in proportion to the allocation of the underlying section 163(j) item. If partnership AB's sole items of income, gain, loss, and deduction were $30 of business interest income, which it allocated solely to A, and $40 of business interest expense, which it allocated $20 to each of A and B, then A and B each would have $15 of deductible business interest expense and $5 of excess business interest expense. In situations where, as in this case, the partnership does not allocate all of its section 163(j) items pro rata this method could require a partnership to allocate its section 163(j) excess items in a manner inconsistent with the Treasury Department and the IRS's resolution of issues four and five. See part VII(A)(1) of this Summary of Comments and Explanation of Revisions section.

Applying the 11-step calculation to the previous example, A would have $20 of deductible business interest expense, and B would have $10 of deductible business interest expense and $10 of excess business interest expense. This result is consistent with the Treasury Department and the IRS's resolution of the five issues described in part VII(A)(1) of this Summary of Comments and Explanation of Revisions section. Because the alternative of allocating section 163(j) excess items in proportion to the allocation of the underlying section 163(j) item could require a partnership to allocate section 163(j) excess items to its partners in a manner that does not attempt to align deductible business interest expense with the ATI and business interest income that supported it at the partnership level (which is inconsistent with the resolution of the five issues described in part VII(A)(1) of this Summary of Comments and Explanation of Revisions section), this alternative is not adopted in the final regulations. Other commenters' similar alternatives were considered and were rejected on the same grounds based on the foregoing analysis.

One commenter recommended another alternative method that, in a more general way than the 11-step calculation, attempts to align deductible business interest expense with the ATI and business interest income that supported such deduction at the partnership level. The commenter stated that this objective could be accomplished as follows. For each partner that is allocated business interest expense, determine the portion of the business interest expense allocated to such partner that would be considered deductible business interest expense, taking into account only the business interest income and ATI allocated to such partner. If the aggregate amount determined for all partners is equal to, or less than, the amount of the partnership's deductible business interest expense, then each partner would be allocated deductible business interest expense in the amount determined in the first step. If the first step produced deductible business interest expense in excess of the limitation determined at the partnership level, each partner's allocation of deductible business interest expense would equal the proportion of the partnership's total deductible business interest expense that the deductible amount determined in the first step for such partner constitutes of the deductible amount determined for all partners. Also, any deductible business interest expense as determined at the partnership level that is not allocated through the first step then would be allocated among the partners that have been allocated business interest deductions in proportion to the amount of business interest expense of each partner remaining after the first step.

The Treasury Department and the IRS do not adopt this alternative method in the final regulations. The commenter's approach provides a method for allocating excess business interest expense, but it does not provide any guidance on allocating excess taxable income or excess business interest income. Further, it is not possible to infer a manner for allocating excess taxable income and excess business interest income from this approach because it fails to distinguish each partner's ATI from its business interest income. By comingling ATI and business interest income in its first step, this method fails to account for the ordering of ATI and business interest income in the partnership context as required by the statute. Section 163(j)(4)(C) provides that partnership ATI does not begin offsetting partnership business interest expense until partnership business interest income has been fully utilized. Because this method is only capable of addressing fact patterns in which there is excess business interest expense, it is not adopted in the final regulations.

Moreover, the Treasury Department and the IRS have concluded that this method for allocating excess business interest expense does not sufficiently reduce taxpayer burden given the trade-off in precision and administrability. To illustrate, the commenter applied its recommended method to the facts of *Example 14* of § 1.163(j)–6(o) of the proposed regulations. In that example, partnership PRS has $140 of business interest expense, $200 of ATI, and no business interest income. Accordingly, PRS has $60 of deductible business interest expense. PRS allocates its items of ATI such that A, B, and C have income of $100, $100, and $400 respectively, while D has a loss of $400. PRS allocates its business interest expense $40 to B, $60 to C, and $40 to D.

Under the suggested method, PRS first would determine for each of B, C, and D the amount of the business interest expense allocated to each partner that would be deductible under section 163(j) taking into account solely the ATI and business interest income allocated to such partner. In this case, the entire $60 of business interest expense allocated to C would have been deductible, $30 of the business interest expense allocated to B would have been deductible, and no amount of business interest expense allocable to D would have been deductible. The total amount of business interest expense determined in the first step (or $90) exceeds the total amount deductible under section 163(j) applied at the partnership level (or $60). PRS then would determine the proportion of the business interest expense allocated to each partner that is determined to be deductible in the first step and allocate the total deduction in those proportions. Thus, C would be entitled to two-thirds ($60/$90) of the $60 deduction ($40 of deductible business interest expense) and B would be entitled to one-third ($30/$90) of the $60 deduction ($20 of deductible business interest expense). D would not be entitled to any business interest expense deduction. Accordingly, B would have $20 of excess business interest expense, C would have $20 of excess business interest expense, and D would have $40 of excess business interest expense.

In contrast, applying the 11-step calculation to the same example results in an allocation of more deductible business interest expense to C ($48) than to B ($12) because C was allocated more ATI ($400) from PRS than B ($100). Unlike the commenter's method, the 11-step calculation increases a partner's amount of deductible business interest expense in response to an increased allocation of ATI and business interest income. The commenter's method allocates deductible business interest expense based on a ratio that does not take into account the fact that C was allocated significantly more ATI from PRS than B. To illustrate this point, consider what would happen in the previous example if the facts were changed so that C was allocated $1,100 of ATI and D was allocated ($1,100) of ATI. Applying the 11-step calculation, C would have $55 of deductible business interest expense. Applying the commenter's method, C's increased allocation of ATI from PRS would have no effect on C's deductible business interest expense—C still would have $40 of deductible business interest expense and $20 of excess business interest expense.

The Treasury Department and the IRS have determined that the 11-step calculation produces the result that is most consistent with the normative principle in the statute that the amount of business interest expense a taxpayer is capable of deducting should increase as its ATI and business interest income increase. Further, the Treasury Department and the IRS view methods that do not increase a partner's amount of deductible business interest expense in response to an increased allocation of ATI from the partnership as less intuitive, and therefore more burdensome in application. Therefore, the final regulations do not adopt commenters' suggested alternative methods.

4. Publicly Traded Partnerships

The Treasury Department and the IRS received comments raising concerns about the continued fungibility of publicly traded partnership (PTP) units if PTPs are required to allocate section 163(j) excess items pursuant to the 11-step calculation. The effect of section 163(j) on the fungibility of PTP units is being addressed in the Concurrent NPRM. Therefore, these issues are not addressed in the final regulations.

5. Pro Rata Exception

Multiple commenters recommended that partnerships that allocate all items of income and expense on a pro rata basis (similar to S corporations) be exempt from the 11-step calculation. Commenters stated that these partnerships by nature do not make the kinds of allocations the 11-step calculation is designed to address. Commenters asserted that simplifying the 11-step calculation for these pro-rata partnerships would reduce complexity and reduce their administrative burden.

The Treasury Department and the IRS agree with these comments. Accordingly, the final regulations provide an exception (pro rata exception) from steps 3 through 11 of the 11-step calculation for partnerships that allocate all section 163(j) items in step 2 proportionately. This pro rata exception will not result in allocations of section 163(j) excess items that vary from the array of allocations of section 163(j) excess items that would have resulted had steps 3 through 11 been performed. See § 1.163(j)–6(f)(2)(ii) and *Example 1* through *Example 16* of § 1.163(j)–6(o).

B. Basis Adjustments

1. Basis and Capital Account Adjustments for Excess Business Interest Expense Allocations

Pursuant to proposed § 1.163(j)–6(f)(2), the adjusted basis of a partner's interest in a partnership is reduced, but not below zero, by the amount of excess business interest expense allocated to the partner. If a partner is subject to a loss limitation under section 704(d) and the partner is allocated losses from a partnership in a taxable year, the limited losses are grouped based on the character of each loss (each grouping of losses based on character, a ''section 704(d) loss class''). If there are multiple section 704(d) loss classes in a given year, the partner apportions the limitation to each section 704(d) loss class proportionately. For purposes of applying this proportionate rule, any deductible business interest expense and business interest expense of an exempt entity (whether allocated to the partner in the current taxable year or suspended under section 704(d) in a prior taxable year), any excess business interest expense allocated to the partner in the current taxable year, and any excess business interest expense from a prior taxable year that was suspended under section 704(d) (negative section 163(j) expense) makes up the same section 704(d) loss class (section 163(j) loss class). Moreover, once the partner determines the amount of limitation on losses apportioned to the section 163(j) loss class, any deductible business interest expense is taken into account before any excess business interest expense or negative section 163(j) expense.

Proposed § 1.163(j)–6(h)(2) provides that negative section 163(j) expense is not treated as excess business interest expense in any subsequent year until such negative section 163(j) expense is no longer suspended under section 704(d). Consequently, an allocation of excess taxable income or excess business interest income does not result in the negative section 163(j) expense being treated as business interest expense paid or accrued by the partner. Further, unlike excess business interest expense, which prevents a partner from including excess taxable income in its ATI as described in section 163(j)(4)(B)(ii) (flush language), negative section 163(j) expense does not affect, and is not affected by, any allocation of excess taxable income to the partner. Accordingly, any excess taxable income allocated to a partner from a partnership while the partner still has a negative section 163(j) expense will be included in the partner's ATI. However, once the negative section 163(j) expense is no longer suspended under section 704(d), it becomes excess business interest expense, which is subject to the general rules in proposed § 1.163(j)–6(g).

Commenters noted that the rule in proposed § 1.163(j)–6(h)(2) is helpful and should be retained in the final regulations. However, commenters further noted that partners with no business interest expense from other sources generally would prefer to treat their negative section 163(j) expense as deductible business interest expense suspended under section 704(d) and utilize excess taxable income in the current year for that purpose, even though the resulting deductible business interest expense would continue to be non-deductible because of a section 704(d) limit. Thus, commenters recommended allowing a partner to use excess taxable income to treat negative section 163(j) expense as deductible business interest expense suspended under section 704(d) instead of using it to increase partner ATI.

The final regulations do not adopt this recommendation. No precedent exists for allowing items suspended under section 704(d) to preemptively clear limitations that apply after section 704(d) while remaining suspended under section 704(d). For example, in the section 469 context, a non-materially participating partner allocated passive income cannot use such passive income to recharacterize passive losses allocated in a previous year as non-passive while those losses remain suspended under section 704(d).

One commenter also recommended adopting a silo approach under section 704(d). Under this approach, if a partner had a section 704(d) limitation, it could bifurcate its items between non-excepted and excepted partnership business items. If the non-excepted portion was net positive, none of the excess business interest expense allocated from the partnership would be negative section 163(j) expense.

However, this approach would be a significant departure from the current rule under section 704(d), which generally requires the limitation on losses under section 704(d) to be allocated to a partner's distributive share of each loss proportionately, regardless of whether such loss is from an excepted or non-excepted trade or business under section 163(j). Moreover, nothing in section 163(j) indicates Congress intended to give excess business interest expense suspended under section 704(d) a better result than any other partnership losses suspended under section 704(d). For that reason, the final regulations do not adopt this recommendation.

2. Basis Adjustments Upon Disposition of Partnership Interests Pursuant to Section 163(j)(4)(B)(iii)(II)

Under the proposed regulations, if a partner disposes of all or substantially all of its partnership interest, the adjusted basis of the partnership interest is increased immediately before the disposition by the entire amount of the remaining excess business interest expense. Following such a disposition, no deduction is permitted to either the transferor or the transferee with respect to the excess business interest expense resulting in the basis increase. If a partner disposes of less than substantially all of its interest in a partnership, the partner cannot increase its basis by any portion of the remaining excess business interest expense. The Treasury Department and the IRS requested comments on this approach in the preamble to the proposed regulations.

Commenters cited multiple concerns with the approach adopted in the proposed regulations. First, commenters claimed that the absence of an excess business interest expense basis addback for a partial disposition of a partnership interest could result in tax gain in excess of economic gain in connection with the sale of a partial interest, while the addition of the entire adjustment to outside basis in connection with a complete disposition could result in economic gain in excess of tax gain. Commenters suggested this timing difference between economic gain and tax gain inappropriately disconnects taxable income from economic income. Second, commenters expressed concern that, because a partial disposition would result in a partner holding a smaller interest in a partnership than it held prior to the partial disposition, the partner would receive smaller allocations of excess taxable income (and excess business interest income) in subsequent years. If none of the excess business interest expense of the partner is affected by the partial disposition, this could extend the amount of time needed for a partner to convert its excess business interest expense to business interest expense treated as paid or accrued. Third, commenters noted that, in the event of a partial disposition of a partnership interest, the proposed regulations may cause a discrepancy between the capital accounts of the transferor and the transferee and the excess business interest expense associated with each partner's interest.

Commenters stated that neither the statute nor its policy of limiting business interest expense deductions calls for the potentially harsh results that could be imposed by the approach provided in the proposed regulations. The main purpose of the excess business interest expense carryover rule is to limit the partner's ability to claim a business interest expense deduction that exceeds the statutory threshold under section 163(j)(1). Commenters stated that this statutory purpose can be accomplished by denying the business interest expense deduction and eliminating the carryforward upon a partial disposition of the partnership interest. In other words, to the extent that a partner foregoes its business interest expense deduction, the purpose of the statute is fulfilled. Thus, a proportionate approach would fulfill the purpose of the statute while not subjecting taxpayers to outcomes that are not plainly contemplated by the statue.

As a solution, commenters recommended that a partial disposition of a partnership interest trigger a proportionate excess business interest expense basis addback and corresponding decrease in such partner's excess business interest expense carryover (proportionate approach). Under the proportionate approach, the partner would be required to track its basis in its partnership interest in a manner similar to that set forth in Revenue Ruling 84–53, 1984–1 C.B. 159 (April 9, 1984). Commenters advocating for a proportionate addback rule varied in their recommendations regarding where the addback should occur. In general, commenters suggested three options: (1) Increase the basis of the partnership interest retained; (2) apportion the basis increase proportionally between the partnership interest retained and the partnership interest being disposed of; and (3) increase the basis of the partnership interest being disposed of.

As described in the preamble to the proposed regulations, the Treasury Department and the IRS originally considered and rejected the proportionate approach. One reason the Treasury Department and the IRS adopted the all or substantially all approach in the proposed regulations over the proportionate approach was because the former appeared more taxpayer-favorable in certain circumstances. Under the all or substantially all approach in the proposed regulations, the excess business interest expense basis addback is delayed for the maximum amount of time (until a partner disposes of all or substantially all of its interest), giving taxpayers more time to receive excess taxable income (and excess business interest income) and thus potentially take an ordinary deduction. However, as commenters pointed out, a smaller partnership interest likely will result in a correspondingly smaller allocation of excess taxable income (and excess business interest income) from the partnership. For this reason, commenters did not perceive the proposed approach as taxpayer-favorable for preserving the possibility of a future ordinary deduction, but rather as taxpayer-unfavorable for delaying what likely will be a capital loss.

Accordingly, the Treasury Department and the IRS adopt the recommended proportionate approach in the final regulations. In the preamble to the proposed regulations, the Treasury Department and the IRS indicated that, if final regulations were to adopt a proportionate approach, such approach would increase the basis of the partnership interest being retained by the amount of the excess business interest expense basis addback. However, upon further consideration, the Treasury Department and the IRS agree with commenters that the basis addback should instead increase the basis of the partnership interest being disposed of. Thus, the final regulations adopt a proportionate approach that increases the basis of the partnership interest being disposed of.

For purposes of § 1.163(j)–6(h)(3), a disposition includes a distribution of money or other property by the partnership to a partner in complete liquidation of its interest in the partnership. The Treasury Department and the IRS request comments on whether a current distribution of money or other property by the partnership to a continuing partner as consideration for an interest in the partnership should also trigger an addback and, if so, how to determine the appropriate amount of the addback. Additionally, the final regulations clarify that each partner is considered to have disposed of its partnership interest within the meaning of § 1.163(j)–6(h)(3) if the partnership terminates under section 708(b)(1).

The proportionate rule adopted in the final regulations applies the equitable apportionment principles of § 1.61–6 (referenced in Revenue Ruling 84–53) to determine the amount of excess business interest expense attributable to the partner's interest sold. In *Example 1* of § 1.61–6, basis is apportioned among properties based on the fair market value of the property and is treated as equitably apportioned. Similarly, in Situations 1 and 3 of Revenue Ruling 84–53, the IRS ruled that a selling partner's basis in the transferred portion of the interest generally equals an amount that bears the same relation to the partner's basis in the partner's entire interest as the fair market value of the transferred portion of the interest bears to the fair market value of the entire interest (the pro rata approach to equitable apportionment). However, if a partnership has liabilities, special adjustments must be made to take into account the effect of the liabilities on the basis of the partner's interest. Accordingly, the final regulations adopt the pro rata approach to equitable apportionment and generally provide that the adjusted basis of the partnership interest being disposed of is increased immediately before the disposition by the amount of the excess business interest expense that is proportionate to the interest disposed of in the transaction.

The Treasury Department and the IRS also received comments recommending the final regulations treat a sale of all or substantially all of a partnership's assets as a deemed disposition of each partner's interest in the partnership within the meaning of section 163(j)(4)(B)(iii)(II). Because the statute requires a disposition of a partnership interest to trigger the basis adjustment described in section 163(j)(4)(B)(iii)(II), the final regulations do not adopt this recommendation.

3. Intercompany Transfer of a Partnership Interest

For a discussion of comments received on intercompany transfers of partnership interests, see part V(D) of this Summary of Comments and Explanation of Revisions section.

C. Debt-Financed Distributions

The treatment of interest expense associated with debt incurred by a partnership or S corporation to finance distributions to owners (debt-financed distributions) is being addressed in the Concurrent NPRM. Therefore, these issues are not addressed in the final regulations.

D. Trading Partnerships

The preamble to the proposed regulations stated that the business interest expense of certain passthrough entities, including S corporations, that are engaged in trades or businesses that are per se non-passive activities and in which one or more owners of the entities do not materially participate within the meaning of section 469, as described in section 163(d)(5)(A)(ii) and as illustrated in Revenue Ruling 2008–12, 2008–1 C.B. 520 (March 10, 2008), will be subject to section 163(j) at the entity level (even if the interest expense is also subject to limitation under section 163(d) at the individual partner level). With respect to partnerships, to the extent that such business interest expense is limited under section 163(j)(4) and becomes a carryover item of partners who do not materially participate with respect to such trades or businesses, those items will be treated as items of investment interest expense in the hands of those owners for purposes of section 163(d) once those carryover items are treated as paid or accrued in a succeeding taxable year. This rule does not apply to corporate partners.

The Treasury Department and the IRS received multiple comments questioning this interpretation of section 163(j)(5) and its interaction with section 163(d)(5)(A)(ii). The interaction of section 163(j)(5) with section 163(d)(5)(A)(ii) is being addressed in the Concurrent NPRM. Therefore, this issue is not addressed in the final regulations.

E. Treatment of Excess Business Interest Expense in Tiered Partnerships

The preamble to the proposed regulations requested comments regarding the application of section 163(j) to tiered partnership structures, and the proposed regulations reserved on this topic. Specifically, the preamble requested comments on whether excess business interest expense should be allocated through upper-tier partnerships and how or when an upper-tier partner's basis should be adjusted when a lower-tier partnership is subject to a section 163(j) limitation. This issue is being addressed in the Concurrent NPRM. Therefore, this issue is not addressed in the final regulations.

F. Partnership Mergers and Divisions

The proposed regulations reserve on guidance regarding the application of section 163(j) to partnership mergers and divisions, and the Treasury Department and the IRS requested comments in the preamble to the proposed regulations on the effect of partnership mergers and divisions on excess business interest expense, excess taxable income, and excepted trade or business elections in the context of section 163(j).

In response to this request, one commenter recommended that: (i) The carryforward rule in proposed § 1.163(j)–6(g) apply to partners of a partnership treated as a continuing partnership in a partnership merger or division; (ii) the disposition rule of proposed § 1.163(j)–6(h)(3)(i) apply to partnership interests that are treated as liquidated in a partnership merger or division; and (iii) the final regulations confirm, perhaps through examples, the application of the excepted trade or business election and termination rules in proposed § 1.163(j)–9 in the context of a partnership merger or division.

The partnership merger and division rules under section 708 may treat a partnership as terminating or continuing, and the regulations under § 1.708–1(c) and (d) provide a construct for analyzing the tax effects of a partnership merger or division. The Treasury Department and the IRS have determined that, in most situations, a partnership merger or division can be analyzed appropriately under the rules of § 1.708–1(c) and (d). As a result, the Treasury Department and the IRS are not providing special rules in the final regulations to analyze the consequences of a partnership merger or division in the context of section 163(j) at this time. However, the Treasury Department and the IRS continue to study these issues.

G. Applicability of Section 382 to S Corporations Regarding Disallowed Business Interest Expense Carryforwards

The proposed regulations provide that sections 381(c)(20) and 382(d)(3) and (k)(1) apply to S corporations with respect to disallowed business expense carryforwards. Proposed § 1.163(j)–6(l)(5) provides that the amount of any business interest expense not allowed as a deduction for any taxable year by reason of the section 163(j) limitation is carried forward in the succeeding taxable year as a disallowed business interest expense carryforward. Proposed

§ 1.163(j)–6(l)(1) provides that any disallowed business interest expense is not allocated to the S corporation's shareholders until such business interest expense is allowed as a deduction under section 163(j). Similarly, under proposed § 1.163(j)–6(l)(6) and (7), an S corporation shareholder's stock basis is reduced, but not below zero, and an S corporation's accumulated adjustments account (AAA) balance is adjusted, when a disallowed business interest expense becomes deductible under section 163(j).

The preamble to the proposed regulations requested comments regarding the proper integration of section 163(j) and section 382 and subchapter S of the Code (subchapter S). In addition, the preamble to the proposed regulations requested comments regarding the treatment of disallowed business interest expense carryforwards as an attribute of the S corporation subject to the section 382 limitation, as opposed to an attribute of the shareholders, and regarding the timing for any adjustments to shareholder basis and the corporation's AAA.

In response, one commenter recommended that the final regulations retain the approach as set forth in the proposed regulations. In particular, the commenter recommended that section 382 (and the comparable provisions of section 383) be applied only to those attributes that are carried forward and taken into account at the corporate level. The commenter contended that it would be appropriate to treat disallowed business interest expense of an S corporation as a ''pre-change loss'' such that the corporation would be a loss corporation pursuant to section 382(k)(1).

The Treasury Department and the IRS agree with the commenter. Because disallowed business interest expense is treated as an attribute of the S corporation, the S corporation's disallowed business interest expense carryforwards will be treated as pre-change losses subject to a section 382 limitation under section 382(d)(3) following an S corporation's ownership change (within the meaning of section 382(g)).

Accordingly, consistent with the treatment of C corporations under section 382, the final regulations provide that a disallowed business interest expense carryforward of an S corporation is treated as pre-change loss and will be subject to a section 382 limitation only if an S corporation undergoes an ownership change within the meaning of section 382(g). For example, under the final regulations, a ''qualifying disposition'' by a shareholder that results in a 20-percent ownership change of the S corporation, on its own, will not cause section 382 to apply to an S corporation upon such qualifying disposition. See § 1.1368–1(g)(2)(i)(A). See also § 1.1368–1(g)(2) (defining the term ''qualifying disposition'').

A commenter also recommended that section 382 not be applied to any item of deduction, loss, or credit that is allocated to shareholders on a current basis and taken into account at the shareholder level. As expressed in the preamble to the proposed regulations, the Treasury Department and the IRS continue to consider the extent to which section 382 should apply to S corporations for purposes other than section 163(j). The application of section 382 to S corporations for purposes of section 163(j) should not be construed as creating any inference regarding the application of section 382 to S corporations for other purposes. The Treasury Department and the IRS continue to seek comments regarding the proper integration of these two Code sections and subchapter S.

H. Separate Application of Section 163(j) Limitation to Short Taxable Years of S Corporation

An S corporation's items of income and loss generally are allocated on a pro rata, per-day basis to all shareholders that hold the corporation's stock during the corporation's taxable year. See section 1377(a)(1). However, subchapter S provides limited exceptions to that general allocation rule. For example, in the event that a shareholder completely terminates its interest, the S corporation and affected shareholders can elect to treat its taxable year ''as if the taxable year consisted of 2 taxable years the first of which ends on the date of the termination'' (each, a hypothetical short taxable year). Section 1377(a)(2)(A). In addition, an S corporation may make such an election if a shareholder has made a qualifying disposition. See § 1.1368–1(g)(2). With regard to each of these instances, the S corporation may elect to ''close the books'' even though the corporation will file one Federal income tax return for the taxable year covering both separate taxable periods.

Subchapter S also specifies instances in which an S corporation may elect, or is required, to file a Federal income tax return for a short taxable year (actual short taxable year). For example, an S corporation may elect to determine taxable income or loss based on a closing-of-the-books method with respect to an S termination year. See section 1362(e)(3) (providing an election to have items assigned to each short taxable year under normal Federal income tax accounting rules). However, if a sale or exchange of at least 50 percent of the S corporation's stock occurs during that S termination year, the S corporation must utilize the closing-of-the-books method. See section 1362(e)(6)(D). See also section 1362(e)(6)(C) (requiring the use of the closing-of-the-books method with respect to any item resulting from the application of section 338).

Based on a request from a commenter, the Treasury Department and the IRS have considered whether the section 163(j) limitation should apply separately with respect to each hypothetical or actual short taxable year. Specifically, the commenter recommended that, if an S corporation (1) has an actual short taxable year, or (2) determines its taxable income or loss as if its taxable year consisted of separate taxable years (that is, hypothetical short taxable years), the final regulations should clarify that a separate section 163(j) limitation should be calculated for, and applied to, each actual or hypothetical short taxable year. To support that recommendation, the commenter emphasized ''sound policy reasons'' for ensuring that owners of the corporation during the first short taxable period are not affected by the fortunes of the corporation during the second short period, and vice versa.

The Treasury Department and the IRS agree that a separate section 163(j) limitation should be calculated for, and applied to, each actual or hypothetical short taxable year. Section 163(j)(1) limits the amount of business interest expense allowed as a deduction ''for any taxable year.'' Accordingly, the Treasury Department and the IRS have determined that a separate section 163(j) limitation should apply to each actual short taxable year. See § 1.1362–3(c)(3) (setting forth the general rule that ''the S and C short years are treated as two separate years for purposes of all provisions of the Internal Revenue Code''). In addition, subchapter S and the regulations in this part under subchapter S explicitly treat hypothetical short taxable years as separate taxable years. See section 1377(a)(2)(A) (providing that an S corporation can treat its taxable year ''as if the taxable year consisted of 2 taxable years'') and § 1.1368–1(g)(1) (providing that the ''section applies as if the taxable year consisted of separate taxable years''). As a result, the Treasury Department and the IRS also have determined that a separate section 163(j) limitation should apply to each hypothetical short taxable year and sections 1.1362–3(c), 1.1368–1(g)(2), and 1.1377–1(b)(3) have been amended accordingly.

I. Partnership or S Corporation Not Subject to Section 163(j)

Under proposed § 1.163(j)–6(m)(1), if a partner or S corporation shareholder is allocated business interest expense from an exempt entity, that allocated business interest expense will be subject to the partner's or S corporation shareholder's section 163(j) limitations. Commenters recommended that proposed § 1.163(j)–6(m)(1) be modified so that business interest expense incurred by a partnership that is an exempt entity is not subject to section 163(j) at the partner level. Commenters argued that proposed § 1.163(j)–6(m)(1) was inconsistent with section 163(j)(4)(A), which requires the testing of partnership-level business interest expense at the partnership level, not the partner level. The Treasury Department and the IRS agree, and have determined that the same argument naturally should apply to S corporations and their shareholders. See section 163(j)(4)(D) (in relevant part, providing that rules similar to section 163(j)(4)(A) shall apply with respect to any S corporation and its shareholders). Accordingly, the final regulations provide that business interest expense of an exempt partnership, or exempt S corporation, pursuant to section 163(j)(3) does not retain its character as business interest expense and, as a result, is not subject to the section 163(j) limitation at the partner or S corporation shareholder level.

One commenter requested clarification as to whether proposed § 1.163(j)–6(m)(3) applies only to exempt entities or also could apply to trades or businesses that become not subject to the requirements of section 163(j) by reason of engaging in excepted trades or businesses. The final regulations clarify that § 1.163(j)–6(m)(3) does not apply when a partnership engages in excepted trades or businesses. Accordingly, if a partner is allocated excess business interest expense from a partnership and, in a succeeding taxable year, such partnership engages in excepted trades or businesses, then the partner shall not treat any of its excess business interest expense that was previously allocated from such partnership as business interest expense paid or accrued by the partner in such succeeding taxable year by reason of the partnership engaging in excepted trades or businesses. Rather, such excess business interest expense shall remain as excess business interest expense until such time as it is treated as business interest expense paid or accrued by the partner pursuant to § 1.163(j)–6(g)(2) or by reason of the partnership becoming an exempt entity. The final regulations provide a similar clarification for S corporations in § 1.163(j)–6(m)(4).

J. Trusts

For purposes of determining ATI for trusts, one commenter noted that the definition of ATI does not contain an addback for deductible trust distributions. Trusts and decedents' estates taxable under section 641 are permitted to deduct under sections 651 and 661 certain distributions made to beneficiaries. The commenter suggested that section 163(j) should apply before a trust takes a deduction for distributions to beneficiaries, and that, if a deductible trust or estate distribution is added back to the trust's ATI and thus is taken into account in determining the amount of interest expense allowable to the trust under section 163(j), such trust or estate distribution should be excluded from the recipient beneficiaries' calculation of ATI. Thus, under the commenter's approach, a beneficiary of a trust or a decedent's estate would not be able to utilize a trust distribution to deduct additional business interest expense at the beneficiary level.

The Treasury Department and the IRS agree with this comment. Proposed Regulation § 1.163(j)–2(f) is consistent with this result. However, in order to clarify that trusts and decedents' estates taxable under section 641 compute ATI without regard to deductions under sections 651 and 661, the final regulations explicitly provide for this positive ATI adjustment. Additionally, the Treasury Department and the IRS have determined that a similar rule should apply for charitable deductions of a trust or a decedent's estate under section 642(c).

K. Qualified Expenditures

The ATI of a partnership is generally determined in accordance with proposed § 1.163(j)–1(b)(1). Partnership ATI is therefore reduced by deductions claimed under sections 173 (relating to circulation expenditures), 174(a) (relating to research and experimental expenditures), 263(c) (relating to intangible drilling and development expenditures), 616(a) (relating to mine development expenditures), and 617(a) (relating to mining exploration expenditures) (collectively, ''qualified expenditures''). As a result, deductions for qualified expenditures will reduce a partnership's section 163(j) limitation pursuant to proposed § 1.163(j)–2(b). Deductions for those items also will reduce the amount of excess taxable income that may be allocated to the partners and thus reduce the amount by which partner-level ATI may be increased under proposed § 1.163(j)–6(e)(1).

A partner may elect to capitalize its distributive share of any qualified expenditures of a partnership under section 59(e)(4)(C) or may be required to capitalize a portion of its distributive share of certain qualified expenditures of a partnership under section 291(b). As a result, the taxable income reported by a partner in a taxable year attributable to the ownership of a partnership interest may exceed the amount of taxable income reported to the partner on a Schedule K–1.

Commenters recommended that a distributive share of partnership deductions capitalized by a partner under section 59(e) or section 291(b) increase the ATI of the partner because qualified expenditures reduce both partnership ATI and excess taxable income but may not reduce the taxable income of a partner. Commenters suggested two different approaches for achieving this result: (1) Adjust the excess taxable income of the partnership, resulting in an increase to partner ATI; and (2) increase the ATI of the partner directly, without making any adjustments to partnership excess taxable income. The interaction of qualified expenditures with section 163(j)(4) is being addressed in the Concurrent NPRM. Therefore, this issue is not addressed in the final regulations.

L. CARES Act Partnership Rules

As discussed in the Background section to this preamble, section 163(j)(10), as amended by the CARES Act, provides a special rule for excess business interest expense allocated to a partner in a taxable year beginning in 2019 (50 percent EBIE Rule). See section 163(j)(10)(a)(ii). The 50 percent EBIE rule is addressed in proposed § 1.163(j)–6(g)(4) of the Concurrent NPRM. The application of the 2019 ATI rule, as provided in section 163(j)(10)(B), in the partnership context is also addressed in proposed § 1.163(j)–6(g)(4) of the Concurrent NPRM. Therefore, the 50 percent EBIE rule and the application of the 2019 ATI rule to partnerships are not addressed in the final regulations.

VIII. Comments on and Changes to Proposed § 1.163(j)–7: Application of the Section 163(j) Limitation to Foreign Corporations and United States Shareholders

Section 1.163(j)–7 provides general rules regarding the application of the section 163(j) limitation to foreign corporations and U.S. shareholders. The following discussion addresses comments relating to proposed § 1.163(j)–7.

The proposed regulations generally apply section 163(j) and the section 163(j) regulations to determine the deductibility of an applicable CFC's business interest expense in the same manner as these provisions apply to determine the deductibility of a domestic C corporation's business interest expense. See proposed § 1.163(j)–7(b)(2). The proposed regulations define an applicable CFC as a CFC in which at least one U.S. shareholder owns stock, within the meaning of section 958(a). However, in certain cases, the proposed regulations limit the amount of an applicable CFC's business interest expense subject to the section 163(j) limitation and modify the computation of an applicable CFC's ATI, respectively. Thus, under the proposed regulations, an applicable CFC with business interest expense applies section 163(j) to determine the extent to which that expense is deductible for purposes of computing subpart F income as defined under section 952, tested income as defined under section 951A(c)(2)(A), and income that is effectively connected with the conduct of a U.S. trade or business (ECI), as applicable. The proposed regulations provide additional guidance for an applicable CFC (and other foreign persons) with ECI in proposed § 1.163(j)-8, as discussed in part IX of this Summary of Comments and Explanation of Revisions section.

The Treasury Department and the IRS requested comments in the preamble to the proposed regulations regarding whether it would be appropriate to provide additional modifications to the application of section 163(j) to applicable CFCs and whether there are particular circumstances in which it may be appropriate to exempt an applicable CFC from the application of section 163(j).

Some commenters recommended that section 163(j) generally should not apply to applicable CFCs. Other commenters suggested that section 163(j) should apply to applicable CFCs only to the extent that they have ECI or, if an income tax treaty applies, business profits attributable to a United States permanent establishment, or to the extent that debt was introduced to an applicable CFC with a principal purpose of avoiding U.S. income taxes. Some commenters argued that the Treasury Department and the IRS lack the authority to apply section 163(j) to applicable CFCs because section 163(j) applies to taxpayers and, they argue, applicable CFCs are not taxpayers. Furthermore, some commenters argued that old section 163(j) did not apply to applicable CFCs and that Congress expressed no intent to change that. Some commenters also argued that applying section 163(j) to applicable CFCs creates significant complexity and an administrative burden. Furthermore, some commenters suggested that applying section 163(j) to applicable CFCs may have a limited effect on tax revenue or that applying section 163(j) to applicable CFCs could, in some cases, result in a net tax benefit to U.S. shareholders.

The Treasury Department and the IRS have determined that, under current law, section 163(j) applies to applicable CFCs and other foreign corporations whose income is relevant for U.S. tax purposes. As a general matter, application of U.S. tax principles to a foreign corporation for purposes of determining its income for U.S. tax purposes is within the authority of the Treasury Department and the IRS. For example, a U.S. shareholder of an applicable CFC takes into account its pro rata share of the subpart F income and net tested income of an applicable CFC. Accordingly, in order to determine the U.S. shareholder's pro rata share, the income of the applicable CFC must be determined. Section 1.952–2(a)(1) provides that, ''[e]xcept as provided in subparagraph (2) of this paragraph [relating to insurance gross income], the gross income of a foreign corporation for any taxable year shall, subject to the special rules of paragraph (c) of this section, be determined by treating such foreign corporation as a domestic corporation taxable under section 11 and by applying the principles of section 61 and the regulations thereunder.'' Neither § 1.952–2(a)(2) nor (c) implicates section 163(j). Accordingly, pursuant to § 1.952–2, a foreign corporation is treated as a domestic corporation for U.S. tax purposes when calculating its taxable income, including by application of section 163(j).

The exclusion of CFCs from the application of old section 163(j) under the 1991 Proposed Regulations is not determinative as to whether applicable CFCs and other foreign corporations should be excluded from the application of section 163(j). Although both old section 163(j) and section 163(j) limit deductions for business interest expense, the policies of each provision are significantly different. Old section 163(j) was a narrower provision that limited a corporation's ability to use interest expense deductions to move earnings out of the United States tax base. Section 163(j) focuses on limiting the potential tax benefit of overleveraged businesses. Because Congress wholly repealed and replaced old section 163(j), the provisions of old section 163(j) and the 1991 Proposed Regulations are not determinative as to the application of section 163(j).

Furthermore, nothing in the Code or legislative history indicates that Congress intended to exclude applicable CFCs or other foreign corporations from the application of section 163(j). Congress expressly provided that section 163(j) should not apply to certain small businesses or to certain excepted trades or businesses. Congress did not exempt applicable CFCs or other foreign corporations from the application of section 163(j).

Accordingly, the final regulations clarify that section 163(j) applies to foreign corporations whose income is relevant for U.S. tax purposes, other than by reason of section 881 or 882 (relevant foreign corporations). Section 1.163(j)–7(b). Furthermore, no comments were received on the application of § 1.952–2 or section 882 for purposes of determining the income, including ECI, of an applicable CFC or on the reduction of an applicable CFC's taxable income by the amount of any dividend received from a related person for purposes of determining ATI. In addition to clarifying that these rules apply to all relevant foreign corporations, the final regulations otherwise adopt these rules unchanged. § 1.163(j)–7(g)(1).

The Treasury Department and the IRS acknowledge that the application of section 163(j) to applicable CFCs and other relevant foreign corporations, like many other tax provisions, will increase the complexity of determining the taxable income of a relevant foreign corporation. Similarly, section 163(j) may have a significant effect on the amount of taxable income of some relevant foreign corporations and have limited or no effect on the amount of taxable income of others. The Treasury Department and the IRS do not view the complexity of a provision of the Code or its net effect on tax revenue as determinative as to whether the provision applies to CFCs. Nonetheless, the Treasury Department and the IRS have determined that it is appropriate to reduce the compliance and administrative burdens of applying section 163(j) to certain applicable CFCs.

Accordingly, the Treasury Department and the IRS have developed new rules, taking into account comments received, that substantially modify the rules contained in proposed § 1.163(j)–7. The Treasury Department and the IRS anticipate that, in many cases, these modifications will significantly reduce the compliance and administrative burdens of applying section 163(j) to applicable CFCs. However, because the operation of these new rules is sufficiently different from the operation of the rules in proposed § 1.163(j)–7, the Treasury Department and the IRS have determined that these rules should be proposed in order to provide taxpayers the opportunity to comment before their finalization. These rules and a discussion of their operation are contained in the Concurrent NPRM.

IX. Comments on and Changes to Section 1.163(j)–8: Application of the Section 163(j) Limitation to Foreign Persons With Effectively Connected Taxable Income.

Proposed § 1.163(j)–8 provides rules for applying section 163(j) to a nonresident alien individual or foreign corporation with ECI. Although no comments were received on proposed § 1.163(j)–8, the Treasury Department and the IRS continue to study methods of determining the amount of deductible business interest expense and disallowed business interest expense carryforwards that are allocable to ECI. Accordingly, the final regulations reserve on the application of the business interest expense deduction limitation to foreign persons with ECI.

In the Concurrent NPRM, the Treasury Department and the IRS are proposing rules for determining the amount of deductible business interest expense and disallowed business interest expense carryforward of a nonresident alien, foreign corporation, or partnership that is properly allocable to ECI. The Treasury Department and the IRS request comments on appropriate methods of making this determination. These comments should consider the appropriate method for determining the extent to which business interest expense determined under § 1.882–5 should be treated as attributable to a partnership and subject to the section 163(j) limitation at the partnership level.

X. Comments on and Changes to Proposed § 1.163(j)–9: Elections for Excepted Trades or Businesses; Safe Harbor for Certain REITs

Section 1.163(j)–9 provides general rules and procedures for making an election for a trade or business to be an electing real property trade or business under section 163(j)(7)(B) and an election for a trade or business to be an electing farming business under section 163(j)(7)(C). The following discussion addresses some of the provisions in § 1.163(j)–9 and the comments received.

A. Protective Elections

Section 163(j)(3) provides that the section 163(j) limitation does not apply to taxpayers that meet the gross receipts test of section 448(c). The small business exemption applies automatically if the requirements are met; thus, no election is necessary to ensure that the section 163(j) limitation does not apply. However, for real property trades or businesses under section 163(j)(7)(B), and for farming businesses under section 163(j)(7)(C), the section 163(j) limitation does not apply only if the taxpayer is eligible for and makes an election.

The preamble to the proposed regulations provides that a taxpayer that qualifies for the small business exemption is not eligible to make an election for a trade or business to be an electing real property trade or business or an electing farming business, in part because the taxpayer is already not subject to the section 163(j) limitation, and in part because an electing real property trade or business or an electing farming business is required to use ADS for certain types of property under section 163(j)(10) and cannot claim the additional first-year depreciation deduction under section 168(k) for those types of property. The Treasury Department and the IRS were concerned that certain small business taxpayers might make the election without realizing that the election could have adverse effects on their deduction for depreciation expense and their method of accounting for depreciation.

Commenters suggested that, in some situations, making an annual gross receipts determination, to determine whether a taxpayer should make an election or is already exempt from the limitation, could be burdensome. For example, a taxpayer that has to request the average annual gross receipts of numerous unrelated entities under section 448 aggregation principles in order to make the gross receipts determination may choose to forgo making that determination if the taxpayer knows that its trade or business qualifies to be an electing real property trade or business or an electing farming business. These commenters requested that taxpayers be allowed to make such an election without regard to whether the gross receipts test of section 448(c) has been tested or is met, notwithstanding the potentially adverse depreciation expense implications.

The Treasury Department and the IRS agree with the commenters. Accordingly, the final regulations provide that taxpayers may make an election for a trade or business to be an electing real property trade or business or an electing farming business, provided that they qualify to make such elections, even if the gross receipts test under section 448(c) may be satisfied by the electing trades or businesses in the taxable year in which the election is made. As is the case for all other electing real property trades or businesses and electing farming businesses, the elections are irrevocable and affect depreciation as provided in section 163(j)(11). However, this rule also benefits taxpayers subject to section 163(j) that are owners of small businesses because treating these small businesses as engaged in an excepted trade or business may result in the allocation of more owner interest expense to excepted trades or businesses under § 1.163(j)–10(c).

Commenters also requested a protective election for taxpayers engaged in rental real estate activities if it is unclear whether the activities rise to the level of a trade or business under section 162. The protective election is necessary, according to some commenters, because the definition of an ''electing real property trade or business'' in section 163(j)(7)(B) and proposed § 1.163(j)–1(b)(14) allows a trade or business described in section 469(c)(7)(C) to make the election, and a real property trade or business as defined in section 469(c)(7)(C) can include rental real estate that does not rise to the level of a section 162 trade or business.

Generally, interest expense associated with an activity that does not rise to the level of a section 162 trade or business is not subject to the section 163(j) limitation. The section 163(j) limitation applies to taxpayers with business interest, which is defined under section 163(j)(5) as any interest properly allocable to a trade or business. Proposed § 1.163(j)–1(b)(38) defines a ''trade or business'' as a trade or business under section 162. In contrast, an electing real property trade or business must be described in section 469(c)(7)(C). Section 1.469–9(b)(1) provides that, for purposes of section 469(c)(7), the term ''trade or business'' is defined as ''any trade or business determined by treating the types of activities in § 1.469–4(b)(1) as if they involved the conduct of a trade or business; and any interest in rental real estate, including any interest in rental real estate that gives rise to deductions under section 212.''

Thus, section 469(c)(7)(C) includes all rental real estate (as defined in § 1.469–9(b)(3)) and adopts a broader definition of a ''trade or business'' than section 162. Under this broader definition, taxpayers with rental real estate may be able to qualify as ''real estate professionals'' through work performed in their rental real estate, even if the rental real estate activities otherwise do not rise to the level of a section 162 trade or business.

For example, for purposes of section 469(c)(7)(C), a taxpayer who owns real property and rents to tenants under a triple net lease arrangement will be treated as engaged in a real property trade or business even though the renting under the terms of a triple net lease arrangement may not rise to the level of a section 162 trade or business. The triple net lease arrangement is included in the broader definition of a trade or business under § 1.469–9(b)(1) because the arrangement represents an interest in rental real estate. Accordingly, renting real property under a triple net lease arrangement generally will fall within the definition of a ''rental real property trade or business'' in section 469(c)(7)(C) and proposed § 1.469–9(b)(2). As a result, the taxpayer with such a rental arrangement should be able to make an election to treat this activity as an electing real property trade or business, if the taxpayer so chooses, even though the renting of real property under a triple net lease arrangement might not be a section 162 trade or business. This result is simply a consequence of Congress cross-referencing the broader section 469 definition of a ''real property trade or business'' for purposes of section 163(j).

Thus, the commenters stated that, although taxpayers who are certain they are not engaged in a section 162 trade or business do not need to make an election out of the section 163(j) limitation because they are not subject to this limitation, taxpayers engaged in rental real estate activities who are not certain whether their rental real estate activities rise to the level of a section 162 trade or business should be given the ability to obtain certainty by making a protective election to treat their rental real estate activities as an electing real property trade or business.

The Treasury Department and the IRS agree with the recommendation for a protective election under these circumstances. Thus, the final regulations provide that an election to treat rental real estate activities as an electing real property trade or business is available regardless of whether the taxpayer making the election is engaged in a trade or business within the meaning of section 162. Under the protective election, a taxpayer engaged in activities described in section 469(c)(7)(C) and § 1.469–9(b)(2), as required in proposed § 1.163(j)–1(b)(14)(i), but unsure whether its activities rise to the level of a section 162 trade or business, may make an election for a trade or business to be an electing real property trade or business.

As with all other electing real property trades or businesses, once the election is made, all other consequences of the election outlined in § 1.163(j)–9 apply, such as the irrevocability of the election and the required use of the alternative depreciation system for certain assets.

B. One-Time Late Election or Withdrawal of Election Procedures

Commenters requested a one-time automatic extension of time for certain taxpayers to file an election under section 163(j)(7)(B) or section 163(j)(7)(C) due to uncertainty about the effect of a decision to make or not make such an election and about which taxpayers are eligible to make such an election prior to the publication of the final regulations. Additionally, commenters requested a one-time opportunity to withdraw an election made under section 163(j)(7)(B) or section 163(j)(7)(C) prior to the publication of the final regulations. The Treasury Department and the IRS agree with the commenters' concerns. Thus, in order to address the commenters' concerns, and to provide immediate transition guidance under section 163(j) for taxpayers affected by the various amendments to the Code made by the CARES Act (including, for example, the technical corrections to section 168(e) of the Code relating to the classification of qualified improvement property), Revenue Procedure 2020–22 was issued to provide an automatic extension of time to make, or an opportunity to withdraw, an election for taxable years beginning in 2018, 2019, or 2020. The revenue procedure also provides the time and manner of making or revoking the three elections provided by the CARES Act under section 163(j)(10) for taxable years beginning in 2019 or 2020.

C. The Anti-Abuse Rule Under Proposed § 1.163(j)–9(h)

Numerous comments were received concerning the anti-abuse rule in proposed § 1.163(j)–9(h)(1) (proposed –9(h) anti-abuse rule). The proposed –9(h) anti-abuse rule prohibits an otherwise qualifying real property trade or business from making an election under section 163(j)(7)(B) if at least 80 percent of the business's real property, determined by fair market value, is leased to a trade or business under common control (that is, 50 percent of the direct and indirect ownership of both businesses is held by related parties within the meaning of sections 267(b) and 707(b)) with the real property trade or business. Proposed § 1.163(j)–9(h)(2) provides an exception to the proposed –9(h) anti-abuse rule for REITs that lease qualified lodging facilities (defined in section 856(d)(9)(D)) and qualified health care properties (defined in section 856(e)(6)(D)) (REIT exception).

The preamble to the proposed regulations explains that it would be inappropriate to allow an election under section 163(j)(7)(B) to be an excepted real property trade or business for a trade or business that leases substantially all of its real property to the owner of the real property trade or business, or to a related party of the owner: ''To permit such an election would encourage a taxpayer to enter into non-economic structures where the real estate components of non-real estate businesses are separated from the rest of such businesses in order to artificially reduce the application of section 163(j) by leasing the real property to the taxpayer or a related party of the taxpayer and electing for this ''business'' to be an excepted real property trade or business. As a result, these proposed regulations would also contain an anti-abuse rule.'' The preamble further explains the reasoning for the REIT exception by stating that, because REITs that lease qualified lodging facilities and qualified healthcare properties are generally permitted (pursuant to section 856(d)(8)(B)) to lease these properties to a taxable REIT subsidiary (TRS), this anti-abuse rule does not apply to these types of REITs. The Treasury Department and the IRS requested comments in the preamble to the proposed regulations on whether other exceptions to the anti-abuse rule (such as, for example, an exception for certain fact patterns where real property that is leased from a related party is ultimately sub-leased to a third party) would be appropriate.

Commenters suggested eliminating or modifying the proposed –9(h) anti-abuse rule because of the concern that, as currently written, this rule applies to non-abusive lease arrangements between commonly controlled trades or businesses. Specifically, commenters raised concerns about the applicability of the proposed –9(h) anti-abuse rule to specific types of business structures where the real property is owned by one legal entity (referred to as property company, or PropCo) and leased to a separate but commonly controlled legal entity that operates and manages a business (referred to as operating company, or OpCo). According to commenters, this PropCo/OpCo structure has valid business protection, lending, and regulatory purposes in certain industries. Commenters also claimed that this structure was in existence for many years prior to the enactment of the section 163(j) limitation and was not created in an attempt to circumvent application of the section 163(j) limitation.

For example, the PropCo/OpCo structure is used by some hotels in the following manner: PropCo generally owns the real property subject to significant debt, services such debt, and leases the real property to OpCo, which operates a real property trade or business by licensing the property to unrelated third parties (guests). This structure is used to limit legal liability, manage state and local tax burdens, plan for family wealth transfers, and for other business objectives. One commenter recommended a ''look-through'' exception to the proposed –9(h) anti-abuse rule where the real property is ultimately leased (or licensed) to unrelated third parties in a PropCo/OpCo structure. This exception would allow a real property trade or business owning real property, or PropCo, to make an election to be an electing real property trade or business if it leases real property to a commonly controlled real property trade or business, or OpCo, if OpCo subleases (or licenses) the real property to unrelated third parties.

Similarly, commenters noted that the property ownership, mortgage, and resulting interest expense for trades or businesses described as nursing homes, continuing care retirement communities, independent living facilities, assisted living facilities, memory care facilities, and skilled nursing facilities (collectively, ''residential living facilities'') is often contained in one legal entity, or PropCo, and the operation and management of the residential living facility is contained in another, commonly controlled legal entity, or OpCo. Commenters explained that the Department of Housing and Urban Development, which is a major lender in the residential living industry, and many other lenders often require the use of single-asset or separate legal entities for lending purposes.

To prevent the application of the proposed –9(h) anti-abuse rule to a PropCo that leases real property to a residential living facility, some commenters suggested that the anti-abuse rule should not apply to a trade or business that leases real property to a residential living facility (1) regardless of whether the lessor and lessee are under common control, or (2) if both the lessor trade or business and the commonly controlled lessee independently qualify as electing real property trades or businesses. Commenters noted that the proposed –9(h) anti-abuse rule should not apply to situations where the entities, if combined or aggregated and without taking the lease into account, would each qualify as real property trades or businesses. Without modification to the proposed –9(h) anti-abuse rule, the PropCo in a PropCo/OpCo structure would be prohibited from making a real property trade or business election even though all of its lease income is derived from a real property trade or business. Commenters suggested that proposed § 1.163(j)–9(h)(2), which provides an exception for REITs, should apply to similarly situated taxpayers that are privately owned but use a commonly controlled entity in a PropCo/OpCo structure rather than a REIT.

Other suggestions made by commenters include (1) eliminating the proposed –9(h) anti-abuse rule and instead relying on the more general proposed § 1.163(j)–2(h) anti-avoidance rule to disregard or recharacterize the types of non-economic structures targeted by the proposed –9(h) anti-abuse rule, (2) clarifying that the proposed –9(h) anti-abuse rule would apply only if there is a ''principal purpose of tax avoidance,'' (3) providing exceptions to the proposed –9(h) anti-abuse rule if the taxpayer demonstrates a substantial economic purpose for the PropCo/OpCo structures unrelated to avoiding section 163(j), or if the PropCo/OpCo structure was in place prior to enactment of the TCJA, and (4) expanding the REIT exception to include all real property trades or businesses that lease to residential living facilities.

The operation of two separate, but commonly controlled, legal entities is also common in the cattle and beef industry—one entity owns all of the land and the buildings used by the operating entity, whereas the operating entity owns inventory (cattle or crops) and equipment and operates the farm, ranch, or feed yard. Commenters recommended providing an exception from the proposed –9(h) anti-abuse rule for farming businesses or, alternatively, clarifying that the allocation rules under proposed § 1.163(j)–10 do not apply to separate out the real property to real property businesses included under the proposed –9(h) anti-abuse rule.

The Treasury Department and the IRS agree with commenters that certain exceptions should be added to the proposed –9(h) anti-abuse rule. The final regulations provide two additional exceptions to the anti-abuse rule. Under the first exception, if at least 90 percent of a lessor's real property, determined by fair market rental value, is leased to a related party that operates an excepted trade or business and/or to unrelated parties, the lessor is eligible to make an election to be an electing real property trade or business for its entire trade or business (de minimis exception). The de minimis exception accommodates taxpayers that, by law or for valid business reasons, divide their real property holding and leasing activities from their operating trade or business that qualifies as an excepted trade or business, while still maintaining an anti-abuse rule to prevent non-economic business structures designed to circumvent the section 163(j) limitation. See § 1.163(j)–9(j).

The second exception is a look-through rule that modifies the proposed –9(h) anti-abuse rule by allowing taxpayers to make an election for a certain portion of their real property trade or business (look-through exception). Under the look-through exception, if a lessor trade or business leases to a trade or business under common control (lessee), the lessor is eligible to make an election to be an electing real property trade or business to the extent that the lessor leases to an unrelated party or to an electing trade or business under common control with the lessor or lessee, and to the extent that the lessee trade or business under common control subleases (or licenses) to unrelated third parties and/or related parties that operate an excepted trade or business. Accordingly, the lessor can make an election for the portion of its trade or business that is equivalent to the portion of the real property that is ultimately leased to unrelated parties and/or related parties that operate an excepted trade or business. A lessor that makes an election under the look-through exception must allocate the basis of assets used in its trades or businesses under the rules provided in § 1.163(j)–10(c)(3)(iii)(D).

D. Residential Living Facilities and Notice With Proposed Revenue Procedure

The PropCo/OpCo structure, discussed previously in part X(C) of this Summary of Comments and Explanation of Revisions section, is used extensively by certain residential living facilities that provide residential housing along with supplemental assistive, nursing, and other routine medical services. The commonly controlled lessees in the PropCo/OpCo structure expressed concern about whether the residential living facility trades or businesses qualify as real property trades or businesses under section 469 and § 1.469–9(b)(2), and are thus eligible to make an election under section 163(j)(7)(B), because of the supplemental services that they provide. Accordingly, Notice 2020—[INSERT NOTICE #], 2020—[INSERT CB/IRB GUIDANCE NUMBERS], released concurrently with these final regulations, provides notice of a proposed revenue procedure detailing a proposed safe harbor under which a taxpayer engaged in a trade or business that manages or operates a residential living facility and that also provides supplemental assistive, nursing, and other routine medical services may elect to treat such trade or business as a real property trade or business within the meaning of section 469(c)(7)(C), solely for purposes of qualifying as an electing real property trade or business under section 163(j)(7)(B). Thus, if a lessor leases real property to a commonly controlled lessee that operates a residential living facility, which qualifies as and makes an election to be an excepted trade or business under the proposed safe harbor in Notice 2020—[INSERT NOTICE #], the lessor may qualify to use the de minimis exception or the look-through exception.

The Treasury Department and the IRS request comments in Notice 2020—[INSERT NOTICE #] on the proposed revenue procedure. Interested parties are invited to submit comments on the proposed revenue procedure by [INSERT DATE 90 DAYS AFTER PUBLICATION of Notice 2020—[INSERT NOTICE #] IN the IRB].

The proposed revenue procedure is proposed to apply to taxpayers with taxable years ending after December 31, 2017. Until such time that the proposed revenue procedure is published in final form, taxpayers may use the safe harbor described in the proposed revenue procedure for purposes of determining whether a residential living facility, as defined in the proposed revenue procedure, may be treated as a real property trade or business solely for purposes of section 163(j).

Future guidance might be needed to determine whether a particular trade or business can make an election. Accordingly, the definitions of electing real property trade or business in § 1.163(j)–1(b)(14) and electing farming business in § 1.163(j)–1(b)(13) include a new provision noting that the Secretary may issue guidance on whether a trade or business can be an electing real property trade or business or electing farming business.

E. Safe Harbor for Certain REITs

Proposed § 1.163(j)–9(g) provides a special safe harbor for REITs. The safe harbor provides that, if a REIT holds real property, interests in partnerships holding real property, or shares in other REITs holding real property, the REIT is eligible to make an election to be an electing real property trade or business for all or part of its assets. If a REIT makes an election to be an electing real property trade or business, and if the value of the REIT's real property financing assets (as defined in proposed § 1.163(j)–9(g)(5) and (6)) at the close of the taxable year is 10 percent or less of the value of the REIT's total assets at the close of the taxable year, then, under the safe harbor in the proposed regulations, all of the REIT's assets are treated as assets of an excepted trade or business. If a REIT makes an election to be an electing real property trade or business, and if the value of the REIT's real property financing assets at the close of the taxable year is more than 10 percent of the value of the REIT's total assets, then, under the safe harbor in the proposed regulations, the REIT's business interest income, business interest expense, and other items of expense and gross income are allocated between excepted and non-excepted trades or businesses under the rules set forth in proposed § 1.163(j)–10, as modified by proposed § 1.163(j)–9(g)(4). The safe harbor also allows REITs to use § 1.856–10 for the definition of ''real property'' in determining which assets are assets of an excepted trade or business. The final regulations generally adopt the safe harbor for REITs in the proposed regulations, with modifications in response to comments discussed in this part X(E) of the Summary of Comments and Explanation of Revisions section.

One commenter recommended that the Treasury Department and the IRS revise proposed § 1.163(j)–9(g)(1) to clarify that a REIT may make the safe harbor election if the REIT owns an interest in one or more partnerships holding real property or stock in one or more REITs holding real property. The commenter indicated that the use of the plural ''interests in partnerships'' and ''shares in other REITs'' could imply that a REIT cannot make the safe harbor election if the REIT owns an interest in a single partnership or shares in a single REIT. The Treasury Department and the IRS agree that the regulations should not preclude a REIT that owns an interest in a single partnership or shares in a single REIT from applying the safe harbor.

This commenter also recommended that the final regulations clarify that the safe harbor election may be made if the electing REIT owns a direct interest in a partnership or lower-tier REIT that does not directly hold real property, but that holds an interest in another partnership or lower-tier REIT that directly holds real property.

The determination of whether a REIT is eligible to make the safe harbor election under the proposed regulations was intended to mirror the determination of whether the REIT holds real property (as defined under § 1.856–10) when testing the value of the REIT's real estate assets under section 856(c)(4)(A). If a REIT is a partner in a partnership that holds real property (as defined under § 1.856–10), the REIT is deemed to own its proportionate share of the partnership's real property for purposes of section 856(c)(4). The Treasury Department and the IRS also recognize that, for purposes of section 856(c)(4), a REIT is deemed to own a share of real property from any partnership interest held through an upper-tier partnership.

Moreover, under section 856(c)(5)(B), shares in other REITs qualify as real estate assets. Although a REIT (shareholder REIT) that holds shares in another REIT would not need to determine whether the other REIT holds real property for purposes of testing the value of the shareholder REIT's real estate assets under section 856(c)(4), the proposed regulations allowed the shareholder REIT to make the safe harbor election as long as it determines that the other REIT holds real property. The Treasury Department and the IRS recognize that the other REIT in this situation may not necessarily hold real property but instead may hold shares in a lower-tier REIT (which is a real estate asset in the hands of the other REIT).

Because the shareholder REIT can hold shares in another REIT that holds shares in a lower-tier REIT that holds real property, the Treasury Department and the IRS have concluded that a shareholder REIT may make the safe harbor election if it determines that it holds an indirect interest in a REIT that holds real property. Accordingly, the final regulations clarify that a REIT may elect to be an electing real property trade or business if the REIT holds real property, interests in one or more partnerships holding real property either directly or indirectly through interests in other partnerships or shares in other REITs, or shares in one or more other REITs holding real property either directly or indirectly through interests in partnerships or shares in other REITs.

Several commenters also requested that certain partnerships with a REIT as a partner be allowed to apply the REIT safe harbor election at the partnership level. Commenters noted that many REITs own interests in partnerships that directly or indirectly hold real property, and these partnerships incur the debt that is secured by the real property and claim the interest expense deductions. Commenters recommended that the REIT safe harbor election be made available to partnerships if: (1) At least one partner is a REIT that owns, directly or indirectly, at least 50 percent of the partnership's capital or profits; (2) the partnership meets the requirements of section 856(c)(2), (3), and (4) as if the partnership were a REIT; and (3) the partnership satisfies the requirements of proposed § 1.163(j)–9(g)(1) as if the partnership were a REIT.

The Treasury Department and the IRS agree that a partnership that is controlled by a REIT or REITs and that would meet the REIT gross income and asset tests in section 856(c)(2), (3), and (4) (as if the partnership were a REIT) is sufficiently similar to a REIT for this purpose. Accordingly, the final regulations provide that a partnership may apply the REIT safe harbor election at the partnership level if one or more REITs own, directly or indirectly, at least 50 percent of the partnership's capital and profits, the partnership meets the requirements of section 856(c)(2), (3), and (4) as if the partnership were a REIT, and the partnership satisfies the requirements described in § 1.163(j)–9(h)(1) as if the partnership were a REIT.

A commenter also recommended that the REIT exception to the proposed § 1.163(j)–9(h) anti-abuse rule be clarified to apply to any partnership in which a REIT owns a 50 percent or greater direct or indirect capital or profits interest, if the partnership leases a qualified lodging facility or qualified health care property to a TRS or a partnership in which a TRS is a 50 percent or greater direct or indirect partner. The REIT exception was intended to allow REITs that lease qualified lodging facilities and qualified healthcare properties pursuant to the related party rental exception in section 856(d)(8)(B) to make a real property trade or business election because these leases are explicitly authorized by the Code. In response to comments, the final regulations clarify that the REIT exception also applies to partnerships making the REIT safe harbor election that lease qualified lodging facilities and qualified healthcare properties. However, the final regulations do not specify the related party to which the REIT must lease the qualified lodging facility or qualified healthcare property in order to qualify for the REIT exception and, therefore, Treasury and the IRS did not include a provision for partnerships in which a TRS is a partner.

A commenter requested clarification regarding the application of the real property trade or business election to a rental real estate partnership and its REIT partners if the partnership holds real property and is not engaged in a trade or business within the meaning of section 162. Part XVI of this Summary of Comments and Explanation of Revision section clarifies that taxpayers engaged in rental real estate activities that do not necessarily rise to the level of a section 162 trade or business nevertheless are treated as engaged in real property trades or businesses within the meaning of section 469(c)(7)(C) (and for purposes of section 163(j) by reference). As such, a partnership engaged in a rental real estate activity (regardless of whether that activity rises to the level of a section 162 trade or business) will be permitted to make the election under section 163(j)(7)(B) with respect to the rental real estate activity to be an electing real property trade or business for purposes of section 163(j), and any interest expense that is allocable to that rental real estate activity and that is allocable to a REIT partner will not be investment interest (within the meaning of section 163(d)) that is treated as interest expense allocable to a trade or business of a C corporation partner under § 1.163(j)–4(b)(3).

For purposes of valuing a REIT's assets, the proposed regulations provide that REIT real property financing assets also include the portion of a shareholder REIT's interest in another REIT attributable to that other REIT's real property financing assets. The final regulations clarify that this rule also applies in the context of tiered-REIT structures.

The proposed regulations provide that no portion of the value of a shareholder REIT's shares in another REIT is included in the value of the shareholder REIT's real property financing assets if all of the other REIT's assets are treated as assets of an excepted trade or business under proposed § 1.163–9(g)(2). The proposed regulations provide that if a shareholder REIT does not receive from the other REIT the information necessary to determine whether and the extent that the assets of the other REIT are investments in real property financing assets, then the shareholder REIT's shares in the other REIT are treated as real property financing assets.

A commenter requested that the final regulations clarify how a shareholder REIT determines whether the value of the other REIT's real property financing assets is 10 percent or less of the other REIT's total asset value for purposes of determining whether the electing shareholder REIT must allocate interest expense between excepted and non-excepted businesses. The commenter recommended that the final regulations provide an example to clarify this point or specify that the shareholder REIT may make this determination based on all of the facts available to the shareholder REIT. The commenter proposed that a shareholder REIT that makes an incorrect determination in good faith that the other REIT qualifies under proposed § 1.163–9(g)(2) nevertheless be permitted to treat all of the value of the lower REIT's shares as assets other than real property financing assets.

In response to this comment, the final regulations allow a shareholder REIT to use an applicable financial statement (within the meaning of section 451(b)) of the other REIT to determine whether and the extent that the assets of the other REIT are investments in real property financing assets (rather than having to receive the information directly from the other REIT). However, the final regulations do not permit a shareholder REIT to treat the shares in the other REIT as assets other than real property financing assets when the shareholder REIT's determination is based on information other than an applicable financial statement or information received directly from the other REIT.

In the event that a REIT is required to allocate its interest expense between excepted and non-excepted trades or businesses under § 1.163(j)–10, a commenter requested clarification regarding the application of the look-through rules to tiered entities. Under the proposed regulations, if a REIT holds an interest in a partnership, in applying the partnership look-through rule in proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*), the REIT also applies the definition of real property under § 1.856–10 to determine whether the partnership's assets are allocable to an excepted trade or business. In addition, under the proposed regulations, if a shareholder REIT holds shares in another REIT and all of the other REIT's assets are not treated as assets of an excepted trade or business, the proposed regulations provide that the shareholder REIT applies the same partnership look-through rule (as if the other REIT were a partnership) in determining the extent to which the shareholder REIT's adjusted basis in the shares of the other REIT is properly allocable to an excepted trade or business of the shareholder REIT.

In response to comments, the final regulations provide that, when applying the partnership look-through rule in the case of tiered entities, a REIT applies the definition of real property in § 1.856–10 to each partnership in the chain to determine whether the partnership's assets are allocable to an excepted trade or business. Furthermore, because shares in other REITs qualify as real estate assets under section 856(c)(5)(B), the final regulations provide that, when applying the look-through rule to REITs within a tiered-entity structure, a shareholder REIT may apply the partnership look-through rule in § 1.163(j)–10(c)(5)(ii)(A)(*2*) to all REITs in the chain.

In response to an informal inquiry, the final regulations also clarify that a REIT or a partnership that is eligible but chooses not to apply the REIT safe harbor election may still elect, under § 1.163(j)–9(b)(1), for one or more of its trades or businesses to be an electing real property trade or business, provided that such trade or business is otherwise eligible to elect under § 1.163(j)–9(b)(1). A REIT or partnership that makes the election under § 1.163(j)–9(b)(1) without utilizing the REIT safe harbor provisions may not rely on any portion of § 1.163(j)–9(h)(1) through (7).

F. Real Property Trade or Business

Proposed § 1.163(j)–10(a)(1)(i) provides that the amount of a taxpayer's interest expense that is properly allocable to excepted trades or businesses is not subject to the section 163(j) limitation, and the amount of a taxpayer's other items of income, gain, deduction, or loss, including interest income, that is properly allocable to excepted trades or businesses is excluded from the calculation of the taxpayer's section 163(j) limitation. Commenters suggested that, for purposes of allocating interest between a non-excepted trade or business and an excepted trade or business, a corporate partner in a partnership that conducts a real property trade or business should be allowed to treat its share of the partnership's real property trade or business as an electing real property trade or business even if the partnership does not make the election.

The Treasury Department and the IRS have rejected this comment because an election under section 163(j)(7)(B) has certain consequences—for example, the use of ADS rather than the general depreciation system for certain types of property, which results in the inability of electing real property trades or businesses to claim the additional first-year depreciation deduction under section 168(k) for those types of property. Therefore, the Treasury Department and the IRS have determined that a corporate partner in a partnership that conducts a real property trade or business should be allowed to treat its share of the partnership's real property trade or business as an electing real property trade or business only if the partnership makes the election. However, see part X(A) of this Summary of Comments and Explanation of Revisions section regarding taxpayers that are eligible to make an election to be an electing real property trade or business but are not certain whether they are engaged in a trade or business under section 162.

XI. Comments on and Changes To Proposed § 1.163(j)–10: Allocation of Interest Expense, Interest Income, and Other Items of Expense and Gross Income to an Excepted Trade or Business.

Section 1.163(j)–10 provides rules for allocating tax items that are properly allocable to a trade or business between excepted trades or businesses and non-excepted trades or businesses for purposes of section 163(j). The following discussion addresses comments relating to proposed § 1.163(j)–10.

A. General Method of Allocation: Asset Basis

Proposed § 1.163(j)–10(c) sets forth the general rule for allocating interest expense and interest income between excepted and non-excepted trades or businesses. Under this general rule, interest expense and interest income is allocated between excepted and non-excepted trades or businesses based upon the relative amounts of the taxpayer's adjusted basis in the assets used in its trades or businesses. As noted in the preamble to the proposed regulations, this general method of allocation reflects the fact that money is fungible and the view that interest expense is attributable to all activities and property, regardless of any specific purpose for incurring an obligation on which interest is paid. Many commenters expressed support for this proposed allocation method.

However, some commenters argued that taxpayers should be permitted to allocate interest expense and income between excepted and non-excepted trades or businesses based on the earnings or gross income of each business, for various reasons. For example, some commenters posited that asset basis may bear little connection to a corporation's borrowing capacity, whereas earnings or revenue are useful indicators of a taxpayer's ability to meet its debt obligations, and earnings are a key factor in determining the amount of debt the taxpayer may borrow and the interest rate the taxpayer will be charged. These commenters also noted that an asset-basis allocation method could yield inconsistent results across industries (for example, industries whose asset mix is heavily skewed towards self-created intangibles will have low asset basis) or within similarly situated industries (if assets are purchased at different times). One commenter also suggested that an earnings-based approach would be easier for the IRS and taxpayers to administer because ATI already must be calculated by each taxpayer that is subject to a section 163(j) limitation.

Although the foregoing arguments have merit, adopting an earnings-based approach would raise many additional considerations, such as taxpayers' ability to time income recognition to affect allocation and create other distortions (as in the case of a trade or business that requires capital investment for a period of years before earning significant gross income). Thus, after further consideration, the Treasury Department and the IRS have decided to retain the asset-basis allocation approach contained in proposed § 1.163(j)–10(c). However, the Treasury Department and the IRS continue to study these comments and may provide future guidance on this issue.

B. Allocation Between Trades or Businesses and Non-Trades or Businesses

Proposed § 1.163(j)–10(a)(2)(i) coordinates the rules under proposed § 1.163(j)–10 with other Federal income tax rules. For example, proposed § 1.163(j)–10(a)(2)(i) provides that, before a taxpayer may determine the amount of interest expense, interest income, or other tax items that is properly allocable to excepted or non-excepted trades or businesses, the taxpayer first must apply § 1.163–8T to determine which tax items are allocable to non-trades or businesses rather than to trades or businesses. Some commenters recommended that non-corporate partners be permitted to allocate tax items between a trade or business and a non-trade or business based on an approach that looks to the earnings of the trade or business and non-trade or business. The commenters argued that an earnings-based approach to determining when debt is properly allocable between a trade or business and a non-trade or business is consistent with determining whether the earnings of a taxpayer can support the level of debt incurred.

After further consideration, the Treasury Department and the IRS have decided to retain the § 1.163–8T tracing approach contained in proposed § 1.163(j)–10(a)(2)(i). However, the Treasury Department and the IRS continue to study these comments and may provide future guidance on this issue. Additionally, the Treasury Department and the IRS are considering issuing additional guidance related to the allocation of interest expense by partnerships or S corporations. See proposed § 1.163–14 in the Concurrent NPRM.

Commenters also recommended that no allocation between business and nonbusiness interest expense be required when a partnership is wholly owned by corporate partners because a corporation can have only business interest income and expense and cannot have investment interest income and expense (see proposed § 1.163(j)–4(b)(3)(i)). The Treasury Department and the IRS have rejected this comment because the recommended approach is inconsistent with the entity approach taken with respect to partnerships in section 163(j)(4). Moreover, a separate rule for partnerships that are wholly owned by corporate partners is subject to manipulation because the partnership could alter the rules to which it is subject simply by admitting a non-corporate partner with a small economic interest in the partnership.

C. Consolidated Groups

1. Overview

As provided in proposed § 1.163(j)–10(a)(4)(i), the computations required by section 163(j) and the section 163(j) regulations generally are made for a consolidated group on a consolidated basis. Thus, for purposes of applying the allocation rules of proposed § 1.163(j)–10, all members of a consolidated group are treated as a single corporation. For example, the group (rather than a particular member) is treated as engaged in excepted or non-excepted trades or businesses. Moreover, intercompany transactions (as defined in § 1.1502–13(b)(1)(i)) are disregarded for purposes of these allocation rules, and property is not treated as used in a trade or business to the extent the use of such property in that trade or business derives from an intercompany transaction. Additionally, stock of a member that is owned by another member of the same consolidated group is not treated as an asset for purposes of § 1.163(j)–10, and the transfer of any amount of member stock to a non-member is treated by the group as a transfer of the member's assets proportionate to the amount of member stock transferred.

After a consolidated group has determined the percentage of the group's interest expense allocable to excepted trades or businesses for the taxable year, this exempt percentage is applied to the interest paid or accrued by each member during the taxable year to any lender that is not a group member. Thus, except to the extent proposed § 1.163(j)–10(d) (providing rules for direct allocation in certain limited circumstances) applies, the same percentage of interest paid or accrued by each member to a lender that is not a member is treated as allocable to excepted trades or businesses, regardless of whether any particular member actually engaged in an excepted trade or business.

2. Intercompany Transactions

Commenters observed that ignoring all intercompany transactions and intercompany obligations for purposes of proposed § 1.163(j)–10 is theoretically simple and generally furthers the single-entity approach adopted elsewhere in the proposed regulations. However, a commenter recommended that taxpayers be permitted to take into account basis from certain intercompany transactions, so long as adequate safeguards are put in place against abuse (for example, to prevent taxpayers from using intercompany transactions to increase the consolidated group's ATI or to shift asset basis to excepted trades or businesses), in order to reduce the administrative burden of tracking asset basis separately for purposes of section 163(j). The commenter also recommended that the Treasury Department and the IRS reconsider whether, in certain circumstances, items from intercompany transactions (other than business interest expense and business interest income) should affect the amount of the consolidated group's ATI.

The Treasury Department and the IRS acknowledge that the approach in proposed § 1.163(j)–10(a)(4)(i) creates an administrative burden for members of consolidated groups. However, this approach is consistent with § 1.1502–13, the stated purpose of which is to prevent intercompany transactions from creating, accelerating, avoiding, or deferring consolidated taxable income or consolidated tax liability (see § 1.1502–13(a)(1)). Allowing tax items from intercompany transactions to affect the calculation of a consolidated group's tentative taxable income and ATI would be inconsistent with the single-entity principles of § 1.1502–13(a). Moreover, taxpayers already must track asset basis information for purposes of § 1.1502–13. Additionally, giving effect to intercompany transactions for purposes of section 163(j) would create other administrative burdens for consolidated group members. See the discussion in part V(B) of this Summary of Comments and Explanation of Revisions section. Thus, the final regulations continue to disregard intercompany transactions for purposes of the allocation rules in proposed § 1.163(j)–10.

3. Use of Property Derives From an Intercompany Transaction

A commenter observed that the meaning of the phrase ''property is not treated as used in a trade or business to the extent the use of such property derives from an intercompany transaction'' is unclear. For example, one member of a consolidated group (S) leases property to another member of the group (B), which uses the property in its trade or business. B's lease with S entitles B to use the property. Should B's use of the property in its trade or business be disregarded for purposes of proposed § 1.163(j)–10 because such use ''derives from an intercompany transaction''?

The Treasury Department and the IRS did not intend for B's use of the property in the foregoing scenario to be disregarded for purposes of the allocation rules in proposed § 1.163(j)–10. If S and B were treated as disregarded entities owned by the same corporation, the lease would be ignored, and the leased property would be treated as an asset used in B's trade or business. The final regulations clarify proposed § 1.163(j)–10(a)(4)(i) to better reflect this intended result.

The commenter also requested confirmation that the same allocation principle applies to third-party costs incurred by members of the group (in other words, that such costs are allocated based on the use of assets in excepted or non-excepted trades or businesses). However, proposed § 1.163(j)–10(b)(5) already provides special rules for the allocation of expenses other than interest expenses. Thus, the final regulations do not adopt this recommendation.

4. Purchase of Member Stock From a Nonmember

A commenter recommended that a purchase by one consolidated group member (S) of stock of another member (or of an entity that becomes a member as a result of the purchase) (in either case, T) from a non-member (X) be treated as a purchase of a proportionate amount of T's assets for purposes of proposed § 1.163(j)–10. Although the proposed regulations treat the transfer of the stock of a member to a non-member as a transfer of a proportionate amount of the member's assets, the proposed regulations do not expressly address the acquisition of the stock of a member (or of a corporation that becomes a member as a result of the acquisition). The commenter noted that, if such acquisitions are not treated as asset purchases, the amount of adjusted basis allocated to an excepted or non-excepted trade or business may differ significantly depending on whether S and T file a consolidated return.

For example, T (which is engaged solely in an excepted trade or business) has assets with a fair market value of $100x and $0 adjusted basis, and $0 liabilities. S (which is engaged solely in a non-excepted trade or business) has $100x adjusted basis in its assets. S purchases 100 percent of T's stock from X for $100x, and S and T do not file a consolidated tax return. As a result, S's stock in T is treated as an asset (under proposed § 1.163(j)–10(c)(5)(ii)(B)) with a basis of $100x. In contrast, if S and T were to file a consolidated return, S's stock in T would not be treated as an asset under proposed § 1.163(j)–10(a)(4). Moreover, it is unclear how much adjusted basis the group could take into account for purposes of the allocation rules. Would the group's adjusted basis in T's assets equal T's basis in its assets immediately before the acquisition (here, $0)? Or would all or some portion of the amount paid by S to acquire T's stock be taken into account? The commenter argued that S should have the same amount of adjusted basis in T's assets regardless of whether S and T file a consolidated return, and that there is no legislative history revealing congressional intent to treat members of a consolidated group and non-consolidated corporations differently in this regard. Thus, according to the commenter, S should be able to take into account the amount paid for its T stock for purposes of the allocation rules in proposed § 1.163(j)–10.

Although Congress did not expressly address this issue, Congress did make clear that the section 163(j) limitation applies at the consolidated group level (see H. Rept. 115–466, at 386 (2017)). Moreover, section 1502 provides broad authority for the Secretary of the Treasury to prescribe regulations to determine the tax liability of a consolidated group in a manner that clearly reflects the income tax liability of the group and that prevents the avoidance of tax liability. Consistent with legislative intent regarding section 163(j) and with the broad grant of authority under section 1502, the proposed regulations treat a consolidated group as a single corporation for purposes of the allocation rules of § 1.163(j)–10, and they disregard the stock of members for purposes of this section.

Additionally, the Treasury Department and the IRS have questions and concerns about treating the acquisition of stock of a member (or of an entity that becomes a member) as an asset sale. How would the purchase price be added to the group's basis in the member's assets, and how would the additional basis added to these assets be depreciated? Would this approach deem the transaction to be an asset acquisition for all Federal income tax purposes or just for purposes of section 163(j), and what complications would arise from treating the transaction as an asset purchase for purposes of section 163(j) but as a stock purchase for other purposes?

Due to concerns about these and other issues, the final regulations do not adopt the commenter's recommendation. However, the Treasury Department and the IRS continue to study the issue raised by the commenter and may address the issue in future guidance.

5. Inclusion of Income From Excepted Trades or Businesses in Consolidated ATI

A commenter noted that, because every member of a consolidated group is treated as engaged in every trade or business of the group for purposes of proposed § 1.163(j)–10, a member engaged solely in an excepted regulated utility trade or business that incurs interest expense related to its business activities will be subject to the section 163(j) limitation if other group members are engaged in non-excepted trades or businesses. The commenter suggested that this outcome is contrary to the policy rationale for the exception for regulated utility trades or businesses. The commenter further noted that the gross income of the excepted trade or business is not included in the group's ATI calculation, and that this outcome could produce anomalous results. The commenter thus recommended that a proportionate share of the gross income of the excepted trade or business be included as an adjustment to consolidated ATI.

The Treasury Department and the IRS do not agree that the results under proposed § 1.163(j)–10(a)(4) are inconsistent with congressional intent or lead to anomalous results. As noted in part XI(C)(4) of this Summary of Comments and Explanation of Revisions section, Congress expressly stated that the section 163(j) limitation applies at the consolidated group level. Thus, the treatment of a consolidated group as a single corporation, and the treatment of every member as engaged in every trade or business of the group, is consistent with congressional intent. Moreover, if the section 163(j) limitation were inapplicable to group members engaged in excepted trades or businesses, consolidated groups could readily avoid the section 163(j) limitation by concentrating their external borrowing in such members. Furthermore, although a portion of the interest expense of a member engaged solely in an excepted trade or business will be subject to the section 163(j) limitation if the group is otherwise engaged in non-excepted trades or businesses, a portion of the interest expense of a member engaged solely in a non-excepted trade or business will not be subject to the section 163(j) limitation if the group is otherwise engaged in excepted trades or businesses—and all of that member's income will factor into the group's ATI calculation. Finally, as the commenter acknowledged, section 163(j)(8)(A)(i) specifically excludes from the determination of ATI any item of income, gain, deduction, or loss that is allocable to an excepted trade or business.

For the foregoing reasons, the Treasury Department and the IRS have determined that no changes to the final regulations are needed with respect to this comment.

6. Engaging in Excepted or Non-Excepted Trades or Businesses as a ''Special Status''

One commenter suggested that the Treasury Department and the IRS consider whether engaging in an excepted trade or business should be treated as a ''special status'' under § 1.1502–13(c)(5) for purposes of applying the intercompany transaction rules of § 1.1502–13.

The intercompany transaction rules apply for purposes of redetermining and allocating attributes under § 1.1502–13(c)(1)(i) in order to reach a ''single entity'' answer under the matching rule of § 1.1502–13(c). For example, one member of a consolidated group is a dealer in securities under section 475 (dealer) and sells a security to a second member that is not a dealer; that second member then sells the security to a nonmember in a later year. The matching rule can apply to ensure that the taxable items of the two members harmonize with regard to timing and character in order to reach the same overall tax treatment that would be given to a single corporation whose two operating divisions engaged in those transactions. See § 1.1502–13(c)(7)(i), *Example 11.*

However, if one member has ''special status'' under § 1.1502–13(c)(5) but the other does not, then attributes of the item would not be redetermined under the matching rule. For example, if S (a bank to which section 582(c) applies) and B (a nonbank) are members of a consolidated group, and if S sells debt securities at a gain to B, the character of S's intercompany gain is ordinary (as required under section 582(c)), but the character of B's corresponding item is determined under § 1.1502–13(c)(1)(i) without the application of section 582(c). See § 1.1502–13(c)(5).

The ''special status'' rules of § 1.1502–13(c)(5) are applicable to entities, such as banks or insurance companies, that are subject to a separate set of Federal income tax rules. Although there are special tax rules for farming, real estate, and utilities, an entity engaged in such trades or businesses also may be engaged in other trades or businesses to which such special tax rules would not apply. Further, the entity's farming, real estate, or utility trade or business need not be its primary trade or business. Moreover, the treatment of excepted trades or businesses as a special status effectively would result in additional tracing of specific items for purposes of § 1.1502–13. As noted in the preamble to the proposed regulations, the Treasury Department and the IRS have decided not to apply a tracing regime to allocate interest expense and income between excepted and non-excepted trades or businesses. Thus, the final regulations do not treat engaging in an excepted trade or business as a special status.

D. Quarterly Asset Testing

Under proposed § 1.163(j)–10(c)(6), a taxpayer must determine the adjusted basis in its assets on a quarterly basis and average those amounts to determine the relative amounts of asset basis for its excepted and non-excepted trades or businesses for a taxable year. In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments on the frequency of asset basis determinations required under proposed § 1.163(j)–10(c).

In response, commenters stated that this quarterly determination requirement is administratively burdensome, and that such a burden is unwarranted because, in many circumstances, measuring asset basis less frequently would produce similar results. Thus, commenters recommended that taxpayers be permitted to allocate asset basis for a taxable year based on the average of adjusted asset basis at the beginning and end of the year. As a result, the ''determination date'' would be the last day of the taxpayer's taxable year, and the ''determination period'' would begin on the first day of the taxpayer's taxable year and end on the last day of the year.

Several commenters recommended that this approach be modeled on the interest valuation provisions in § 1.861–9T(g)(2)(i). Under these rules, taxpayers generally must compute the value of assets based on an average of asset values at the beginning and end of the year. However, if a ''substantial distortion'' of asset values would result from this approach (for example, if there is a major acquisition or disposition), the taxpayer must use a different method of asset valuation that more clearly reflects the average value of assets.

Other commenters suggested that their proposed approach could be limited to cases in which there is no more than a de minimis change in asset basis between the beginning and end of the taxable year. For example, this approach could be available for a taxable year only if the taxpayer demonstrates that its total adjusted basis (as measured in accordance with the rules in proposed § 1.163(j)–10(c)(5)) at the end of the year in its assets used in its excepted trades or businesses, as a percentage of the taxpayer's total adjusted basis at the end of such year in all of its assets used in a trade or business, does not differ by more than 10 percent from such percentage at the beginning of the year.

The Treasury Department and the IRS acknowledge that determining asset basis on a quarterly basis would impose an administrative burden. The Treasury Department and the IRS also agree with commenters that a safeguard is needed to account for episodic events, such as acquisitions, dispositions, or changes in business, that could affect average values. Thus, the final regulations permit a taxpayer to compute asset basis in its excepted and non-excepted trades or businesses by averaging asset basis at the beginning and end of the year, so long as the taxpayer falls under a 20 percent de minimis threshold.

E. De Minimis Rules

1. Overview

The proposed regulations provide a number of de minimis rules to simplify the application of § 1.163(j)–10. For example, proposed § 1.163(j)–10(c)(3)(iii)(C)(*3*) provides that a utility trade or business is treated entirely as an excepted regulated utility trade or business if more than 90 percent of the items described in proposed § 1.163(j)–1(b)(15) are furnished or sold at rates qualifying for the excepted regulated utility trade or business exception. Proposed § 1.163(j)–10(c)(3)(iii)(B)(*2*) provides that, if 90 percent or more of the basis in an asset would be allocated under proposed § 1.163(j)–10(c)(3) to either excepted or non-excepted trades or businesses, then the entire basis in the asset is allocated to either excepted or non-excepted trades or businesses, respectively. In turn, proposed § 1.163(j)–10(c)(1)(ii) provides that, if 90 percent or more of a taxpayer's basis in its assets is allocated under proposed § 1.163(j)–10(c) to either excepted or non-excepted trades or businesses, then all of the taxpayer's interest expense and interest income are allocated to either excepted or non-excepted trades or businesses, respectively.

2. Order in Which the De Minimis Rules Apply

A commenter recommended that these de minimis rules be applied in the order in which they are listed in the foregoing paragraph. In other words, a taxpayer first should determine the extent to which its utility businesses are excepted regulated utility trades or businesses. The taxpayer then should determine the extent to which the basis of any assets used in both excepted and non-excepted trades or businesses should be wholly allocated to either excepted or non-excepted trades or businesses. Only then should the taxpayer determine whether all of its interest expense and interest income should be wholly allocated to either excepted or non-excepted trades or businesses. The Treasury Department and the IRS agree that the order recommended by the commenter is the most reasonable application of these de minimis rules, and the final regulations adopt language confirming this ordering.

3. Mandatory Application of De Minimis Rules

Commenters also requested that the final regulations continue to mandate the application of the foregoing de minimis rules rather than make such de minimis rules elective. The commenters expressed concern that creating an election to use the de minimis rules in § 1.163(j)–10(c)(1) and (3) would create uncertainty for taxpayers, and they argued that mandatory application of the de minimis rules would simplify the rules for taxpayers. The Treasury Department and the IRS agree that mandatory application of the de minimis rules simplifies the application of § 1.163(j)–10 and eases the burdens of compliance and administration. Therefore, the final regulations continue to mandate the application of the de minimis rules in § 1.163(j)–10(c)(1) and (3).

4. De Minimis Threshold for Electric Cooperatives

A commenter requested that the de minimis threshold for utilities in proposed § 1.163(j)–10(c)(3)(iii)(C)(*3*) be lowered from 90 percent to 85 percent for electric cooperatives. The commenter argued that a different threshold is appropriate for electric cooperatives because, under section 501(c)(12), 85 percent or more of an electric cooperative's income (with adjustments) must consist of amounts collected from members for the sole purpose of meeting losses and expenses in order for the cooperative to be exempt from Federal income tax.

The Treasury Department and the IRS have determined that the final regulations should provide the same de minimis threshold for electric cooperatives as for other utility trades or businesses. The 85 percent threshold under section 501(c)(12) measures a cooperative's income, with adjustments that are specific to section 501. Moreover, an electric cooperative is not required to qualify for tax exemption under section 501(c)(12) to be engaged in an excepted regulated utility trade or business. Therefore, the Treasury Department and the IRS have determined that the nexus between section 501(c)(12) and proposed § 1.163(j)–10 is insufficient to justify lowering the utility de minimis threshold to 85 percent for electric cooperatives, and the final regulations do not incorporate the commenter's suggestion.

5. Standardization of 90 Percent De Minimis Tests

The terminology used in the 90 percent de minimis tests in proposed § 1.163(j)–10 is not consistent. For example, proposed § 1.163(j)–10(c)(3)(iii)(C)(*3*) uses a ''more than 90 percent'' standard, whereas proposed § 1.163(j)–10(c)(3)(iii)(B)(*2*) uses a ''90 percent or more'' standard. For the sake of consistency, and in order to minimize confusion, the final regulations standardize the language used in these tests.

6. Overlapping De Minimis Tests

In addition to the de minimis tests previously described in this part XI(E) of the Summary of Comments and Explanation of Revisions section, proposed § 1.163(j)–10(c)(3)(iii)(B)(*1*) also contains another de minimis rule. Under this rule, if at least 90 percent of gross income generated by an asset during a determination period is with respect to either excepted or non-excepted trades or businesses, then the entire basis in the asset is allocated to either excepted or non-excepted trades or businesses, respectively.

The Treasury Department and the IRS have determined that this rule not only overlaps with, but also may yield results inconsistent with, the de minimis rule in § 1.163(j)–10(c)(3)(iii)(B)(*2*). Thus, the final regulations eliminate the de minimis rule in proposed § 1.163(j)–10(c)(3)(iii)(B)(*1*).

F. Assets Used in More Than One Trade or Business

1. Overview

Proposed § 1.163(j)–10(c)(3) contains special rules for allocating basis in assets used in more than one trade or business. In general, if an asset is used in more than one trade or business during a determination period, the taxpayer's adjusted basis in the asset must be allocated to each trade or business using one of three permissible methodologies, depending on which methodology most reasonably reflects the use of the asset in each trade or business during that determination period. These three methodologies are: (i) The relative amounts of gross income that an asset generates, has generated, or may reasonably be expected to generate, within the meaning of § 1.861–9T(g)(3), with respect to the trades or businesses; (ii) if the asset is land or an inherently permanent structure, the relative amounts of physical space used by the trades or businesses; and (iii) if the trades or businesses generate the same unit of output, the relative amounts of output of those trades or businesses. However, taxpayers must use the relative output methodology to allocate the basis of assets used in both excepted and non-excepted utility trades or businesses.

As described in part XI(E)(1) of this Summary of Comments and Explanation of Revisions section, a taxpayer's allocation of basis in assets used in more than one trade or business is subject to several de minimis rules (see proposed § 1.163(j)–10(c)(3)(iii)).

2. Consistency Requirement

A commenter requested clarification that the consistency requirement in proposed § 1.163(j)–10(c)(3)(iii)(A) does not require a taxpayer to use a single methodology for different categories of assets, because a methodology that is reasonable for one type of asset (for example, office buildings) may not be reasonable for another (for example, intangibles). The Treasury Department and the IRS agree with this comment, and the final regulations have been clarified accordingly.

3. Changing a Taxpayer's Allocation Methodology

The Treasury Department and the IRS have determined that requiring taxpayers to obtain consent from the Commissioner to change their allocation methodology would impose an undue burden. Thus, the final regulations permit a taxpayer to change its allocation methodology after a period of five taxable years without obtaining consent from the Commissioner. A taxpayer that seeks to change its allocation methodology more frequently must obtain consent from the Commissioner.

The Treasury Department and the IRS also have determined that an allocation methodology is not a method of accounting because there is no guarantee that a taxpayer will be able to deduct a disallowed business interest expense carryforward in future taxable years (as a result, there could be a permanent disallowance). See the discussion in part III(A) of this Summary of Comments and Explanation of Revisions section.

4. Mandatory Use of Relative Output for Utility Trades or Businesses

A commenter requested that the final regulations allow electric cooperatives to use methodologies other than relative output to allocate the basis of assets used in both excepted and non-excepted utility trades or businesses. The commenter noted that alternative methods, such as allocations based on dollars of sales (or sales less the cost of sales), have been allowed by the IRS in the context of allocating expenses between patronage and non-patronage sales. The commenter also stated that economic realities facing electric cooperatives operating on a not-for-profit basis would not be accurately reflected by a relative output methodology.

The Treasury Department and the IRS have concluded that relative output most reasonably reflects the use of assets in excepted and non-excepted utility trades or businesses because § 1.163(j)–1(b)(15)(i)(A) divides utility businesses into excepted regulated utility trades or businesses and non-excepted utility businesses on the same basis. To the extent that items described in § 1.163(j)–1(b)(15)(i)(A) are sold at rates described in § 1.163(j)–1(b)(15)(i)(B), and to the extent that the trade or business is an electing regulated utility trade or business under § 1.163(j)–1(b)(15)(iii), a utility trade or business is an excepted trade or business. The Treasury Department and the IRS do not agree that the final regulations should apply one methodology for differentiating excepted and non-excepted utility trades or businesses under § 1.163(j)–1 and a different methodology to determine the allocation of an asset's basis between such businesses. Therefore, the final regulations do not incorporate the commenter's suggestion.

Another commenter recommended that the rule mandating the use of relative output for the allocation of asset basis under proposed § 1.163(j)–10(c)(3)(iii)(C)(*2*) not be used either to allocate assets used exclusively in excepted or non-excepted utility trades or businesses or to apply the de minimis test of proposed § 1.163(j)–10(c)(1)(ii).

The special rule in proposed § 1.163(j)–10(c)(3)(iii)(C)(*2*) mandates the use of relative output only for the purpose of allocating the basis of assets used in both excepted and non-excepted utility trades or businesses. Therefore, the rule does not mandate the use of relative output to allocate the basis of an asset that is used solely in either an excepted regulated utility trade or business or a non-excepted utility trade or business, except to the extent the de minimis rule in proposed § 1.163(j)–10(c)(3)(iii)(C)(*3*) treats a taxpayer's entire trade or business as either an excepted trade or business or a non-excepted trade or business. The language proposed by the commenter still subjects assets to the de minimis rule in proposed § 1.163(j)–10(c)(3)(iii)(C)(*3*). Because the proposed regulations achieve the result requested by the commenter, the final regulations do not adopt the recommended change.

The de minimis rule in proposed § 1.163(j)–10(c)(1)(ii) applies only after the basis of assets has been allocated between excepted and non-excepted trades or businesses. This de minimis rule treats all of a taxpayer's trades or businesses as either excepted or non-excepted trades or businesses based on such allocation. Because the rule of proposed § 1.163(j)–10(c)(1)(ii) does not apply the methodologies listed in proposed § 1.163(j)–10(c)(3), including the relative output methodology, no change to the proposed regulations is necessary to achieve the result requested by the commenter with respect to proposed § 1.163(j)–10(c)(1)(ii).

G. Exclusions From Basis Calculations

For purposes of allocating interest expense and interest income under the asset-basis allocation method in proposed § 1.163(j)–10(c), a taxpayer's basis in certain types of assets generally is not taken into account. These assets include cash and cash equivalents (see proposed § 1.163(j)–10(c)(5)(iii)). As noted in the preamble to the proposed regulations, this rule is intended to discourage taxpayers from moving cash to excepted trades or businesses to increase the amount of asset basis therein. In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments on this special rule, including whether any exceptions should apply (such as for working capital).

In response, commenters recommended that working capital be included in the basis allocation determination, along with collateral that secures derivatives that hedge business assets and liabilities within the meaning of § 1.1221–2.

The Treasury Department and the IRS have concluded that the inclusion of working capital in the basis allocation determination could lead to frequent disputes between taxpayers and the IRS over the amount of cash that comprises ''working capital'' and the allocation of such amount between and among a taxpayer's excepted and non-excepted trades or businesses. Thus, the final regulations do not adopt this recommendation.

The Treasury Department and the IRS also have concluded that the inclusion of collateral that secures derivatives that hedge business assets and liabilities within the meaning of § 1.1221–2 could lead to frequent disputes between taxpayers and the IRS for reasons similar to those for working capital. For example, it is not always clear which business asset or liability is being hedged, especially in the case of an aggregate hedging transaction. In addition, taxpayers could use this rule as a planning opportunity for purposes of allocating the collateral to excepted trades or businesses. Thus, the final regulations also do not adopt this recommendation.

H. Look-Through Rules

1. Ownership Thresholds; Direct and Indirect Ownership Interests

Proposed § 1.163(j)–10(c)(5)(ii) provides, in part, that if a taxpayer owns an interest in a partnership or stock in a corporation that is not a member of the taxpayer's consolidated group, the partnership interest or stock is treated as an asset of the taxpayer for purposes of the allocation rules of proposed § 1.163(j)–10.

For purposes of allocating a partner's basis in its partnership interest between excepted and non-excepted trades or businesses under proposed § 1.163(j)–10, the partner generally may look through to its share of the partnership's basis in the partnership's assets (with certain modifications and limitations) regardless of the extent of the partner's ownership interest in the partnership. However, the partner must apply this look-through rule if its direct and indirect interest in the partnership is greater than or equal to 80 percent. Similar rules apply to shareholders of S corporations. See proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*i*) and (c)(5)(ii)(B)(*3*)(*ii*).

For purposes of allocating a shareholder's stock basis between excepted and non-excepted trades or businesses, a shareholder of a domestic non-consolidated C corporation or a CFC also must look through to the assets of the corporation if the shareholder's direct and indirect interest therein satisfies the ownership requirements of section 1504(a)(2). Shareholders of domestic non-consolidated C corporations and CFCs may not look through their stock in such corporations if they do not satisfy this ownership threshold. See proposed § 1.163(j)–10(c)(5)(ii)(B)(*2*)(*i*) and (c)(7)(i)(A).

If a shareholder receives a dividend that is not investment income, and if the shareholder looks through to the assets of the payor corporation under proposed § 1.163(j)–10(c)(5)(ii) for the taxable year, the shareholder also must look through to the activities of the payor corporation to allocate the dividend between the shareholder's excepted and non-excepted trades or businesses. See proposed § 1.163(j)–10(b)(3) and (c)(7)(i)(B).

Commenters recommended that taxpayers be afforded greater flexibility to look through their stock in domestic non-consolidated C corporations and CFCs. For example, one commenter suggested that the look-through threshold for CFCs be lowered to 50 percent (analogous to the look-through threshold for related CFCs in section 954(c)(6)). Another commenter recommended that a taxpayer be allowed to look through its stock in a domestic non-consolidated C corporation if the taxpayer owns at least 80 percent of such stock by value, regardless of whether the taxpayer also owns 80 percent of such stock by vote. Yet another commenter recommended that a taxpayer be allowed to look through its stock in a domestic non-consolidated C corporation (or be allowed to allocate its entire basis in such stock to an excepted trade or business) if (i) the taxpayer and the C corporation are engaged in the same excepted trade or business, and (ii) the taxpayer either (A) owns at least 50 percent of the stock of the C corporation, or (B) owns at least 20 percent of the stock of the C corporation and exercises a significant degree of control over the corporation's trade or business. Another commenter recommended that the ownership threshold for looking through domestic non-consolidated C corporations and CFCs be eliminated entirely so that interest expense paid or accrued on debt incurred to finance the acquisition of a real estate business is exempt from the section 163(j) limitation (if the business qualifies for and makes an election under proposed § 1.163(j)–9), regardless of whether that business is held directly or through a subsidiary.

The Treasury Department and the IRS have determined that a de minimis ownership threshold is appropriate for domestic non-consolidated C corporations and CFCs because, unlike a partnership, a corporation generally is respected as an entity separate from its owner(s) for tax purposes. See, for example, *Moline Properties* v. *Commissioner,* 319 U.S. 436 (1943). The look-through rule for non-consolidated C corporations provides a limited exception to this general rule. Moreover, unlike S corporations, domestic C corporations are not taxed as flow-through entities. Thus, the final regulations retain an 80 percent ownership threshold for looking through a domestic non-consolidated C corporation or a CFC.

However, the final regulations permit a taxpayer to look through its stock in a domestic non-consolidated C corporation or a CFC if the taxpayer owns at least 80 percent of such stock by value, regardless of whether the taxpayer also owns at least 80 percent of such stock by vote. Corresponding changes have been made to the look-through rule for dividends.

Additionally, the final regulations permit a shareholder that meets the ownership requirements for looking through the stock of a domestic non-consolidated C corporation (determined without applying the constructive ownership rules of section 318(a)) to look through to such shareholder's pro rata share of the C corporation's basis in its assets for purposes of § 1.163(j)–10(c) (asset basis look-through approach). If a shareholder applies the asset basis look-through approach, it must do so for all domestic non-consolidated C corporations for which the shareholder is eligible to use this approach, and it must continue to use the asset basis look-through approach in all future taxable years in which the shareholder is eligible to use this approach.

Commenters also asked for clarification as to the meaning of an ''indirect'' interest for purposes of these look-through rules. For example, commenters asked what the term ''indirect'' means in the context of the look-through rule for dividends. Commenters further noted that, because section 1504(a)(2) does not contain constructive ownership rules, there is uncertainty as to when a shareholder's indirect ownership in a corporation is counted for purposes of the ownership requirement in the look-through rule. Commenters also requested specific constructive ownership rules, as well as examples to illustrate the application of the ''direct or indirect'' ownership threshold.

The Treasury Department and the IRS have determined that, for purposes of applying the ownership thresholds in § 1.163(j)–10(c)(5)(ii)(B)(*2*)(*i*), (c)(5)(ii)(B)(*3*)(*ii*), and (c)(7)(i)(A) to shareholders of domestic non-consolidated C corporations, CFCs, and S corporations, as applicable, the constructive ownership rules of section 318(a) should apply. For example, assume A, B, and C are all non-consolidated C corporations; A wholly and directly owns B; A and B each directly own 50 percent of C; A and B both conduct a non-excepted trade or business; and C conducts an excepted trade or business. Under section 318(a)(2)(C), A is considered to own the stock owned by B. As a result, A is considered to own 100 percent of the stock of C, and the look-through rule of proposed § 1.163(j)–10(c)(5)(ii)(B)(*2*)(*i*) and (c)(7)(i)(A) applies to A's stock in C. Thus, although the Treasury Department and the IRS have determined that the ownership threshold for non-consolidated C corporations should remain at 80 percent, the constructive ownership rules of section 318 will broaden the availability of the look-through rules to shareholders of such corporations.

In contrast, the Treasury Department and the IRS have determined that the constructive ownership rules of section 318(a) should not apply for purposes of applying the ownership threshold in proposed § 1.163(j)–10(b)(3) and (c)(7)(i)(B) to the receipt of dividends from domestic C corporations and CFCs because dividends are not paid to indirect shareholders. To avoid confusion in this regard, the final regulations remove the word ''indirect'' from the ownership threshold for the dividend look-through rule.

2. Application of Look-Through Rules to Partnerships

i. In General

For purposes of proposed § 1.163(j)–10(c), a partnership interest is treated as an asset of the partner. Pursuant to proposed § 1.163(j)–10(c)(5)(ii)(A)(*1*), the partner's adjusted basis in its partnership interest is reduced, but not below zero, by the partner's share of partnership liabilities as determined under section 752 (section 752 basis reduction rule). Pursuant to proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*iii*), a partner other than a C corporation or tax-exempt corporation must further reduce its adjusted basis in its partnership interest by its share of the tax basis of partnership assets that is not properly allocable to a trade or business (investment asset basis reduction rule).

As noted in part XI(H)(1) of this Summary of Comments and Explanation of Revisions section, a partner may determine what portion of its adjusted tax basis in a partnership interest is attributable to an excepted or non-excepted trade or business by reference to its share of the partnership's basis in the partnership's assets (look-through rule). Under proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*i*), a partner generally may choose whether to apply the look-through rule without regard to its ownership percentage, with two exceptions. First, if a partner's direct or indirect interest in a partnership is greater than or equal to 80 percent of the partnership's capital or profits, the partner must apply the look-through rule. Second, if the partnership is eligible for the small business exemption under section 163(j)(3) and proposed § 1.163(j)–2(d)(1), a partner may not apply the look-through rule.

Proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*ii*) provides that if, after applying the investment asset basis reduction rule, at least 90 percent of a partner's share of a partnership's basis in its assets (including adjustments under sections 734(b) and 743(b)) is allocable to either excepted or non-excepted trades or businesses, the partner's entire basis in its partnership interest is treated as allocable to such excepted or non-excepted trades or businesses.

Pursuant to proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*iv*), if a partner, other than a C corporation or a tax-exempt corporation, does not apply the look-through rule, the partner generally will treat its basis in the partnership interest as either an asset held for investment or a non-excepted trade or business asset as determined under section 163(d).

ii. Coordination of Look-Through Rule and Basis Determination Rules

Outside of the partnership context, proposed § 1.163(j)–10(c)(5)(i) provides rules regarding the computation of adjusted basis for purposes of allocating business interest expense between excepted and non-excepted trades or businesses (collectively, the ''basis determination rules''). For example, proposed § 1.163(j)–10(c)(5)(i)(A) generally provides that the adjusted basis of non-depreciable property other than land is the adjusted basis of the asset used for determining gain or loss from the sale or other disposition of that asset as provided in § 1.1011–1, and proposed § 1.163(j)–10(c)(5)(i)(C) generally provides that the adjusted basis of land and inherently permanent structures is its unadjusted basis. For purposes of applying the look-through rule, the Treasury Department and the IRS intended the basis determination rules to require adjustments to the partnership's basis in its assets and the partner's basis in its partnership interest to the extent of the partner's share of any adjustments to the basis of the partnership's assets. Accordingly, the final regulations explicitly provide that such is the case.

Multiple commenters noted that the proposed regulations do not specify whether a partner that does not apply the look-through rule should use the adjusted tax basis in its partnership interest or should adjust its tax basis to reflect what its basis would be if the partnership applied the basis determination rules to its assets. Because all partnerships are not subject to section 163(j) and cannot provide all partners with the information necessary to adjust the tax basis of their partnership interests consistent with the basis determination rules, the Treasury Department and the IRS have determined that the basis determination rules should not apply to the basis of a partnership interest if a partner does not apply the look-through rule.

iii. Applying the Look-Through Rule and Determining Share of Partnership Basis

Proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*i*) provides that, for purposes of the look-through rule, a partner's share of a partnership's assets is determined using a reasonable method, taking into account special allocations under section 704(b), adjustments under sections 734(b) and 743(b), and direct adjustments relating to assets subject to qualified nonrecourse indebtedness under proposed § 1.163(j)–10(d)(4). Commenters argued that this language does not provide adequate guidance regarding how a partner should determine its share of the tax basis of a specific partnership asset when applying the look-through rule. The commenters stated that, by indicating that sections 743(b) and 704(b) should be taken into account, the proposed regulations imply that a partner's share of the partnership's basis in an asset is determined by reference to the future depreciation deductions that a partner would be allocated with regard to such asset or the amount of basis to be taken into account by that partner in determining its allocable share of gain or loss on the partnership's disposition of the asset. The commenters also requested that final regulations address whether and how allocations under section 704(c) affect a partner's share of the partnership's basis in its assets. After further consideration, the Treasury Department and the IRS have decided to retain the rule in proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*i*).

iv. Investment Asset Basis Reduction Rule

Under proposed § 1.163(j)–10(c)(5)(ii)(A)(*2*)(*iii*), for purposes of applying the investment asset basis reduction rule, a partner's share of a partnership's assets is determined under a reasonable method, taking into account special allocations under section 704(b). A commenter recommended clarifying whether the investment asset basis reduction should be made in accordance with a partner's share of the partnership's actual adjusted basis in an asset or in accordance with the partner's share of the partnership's basis in an asset as determined pursuant to the basis determination rules. The commenter further recommended that the approach adopted on this issue should be consistent with the approach adopted for purposes of determining a partner's adjusted basis in its partnership interest.

The Treasury Department and the IRS agree that these two rules should be applied consistently. After further consideration, the Treasury Department and the IRS have decided to retain the rule that allows a partner's share of a partnership's investment assets to be determined using a reasonable method, taking into account special allocations under section 704(b). However, if a partner elects to apply the look-through rule, then the partner also must apply the basis determination rules. If a partner elects not to apply, or is precluded from applying, the look-through rule, then the approach the partner uses for purposes of the investment asset basis reduction rule must be consistent with the approach the partner uses to determine the partner's adjusted basis in its partnership interest.

v. Coordination of Section 752 Basis Reduction Rule and Investment Asset Basis Reduction Rule

Multiple commenters noted that the combined effect of the section 752 basis reduction rule and the investment asset basis reduction rule could require a partner, other than a C corporation or a tax-exempt corporation, in a partnership that holds investment assets funded by partnership liabilities to reduce the adjusted tax basis of its partnership interest twice—once for the partnership's basis in its investment assets, and a second time for the liabilities that funded their purchase. The Treasury Department and the IRS have determined that this result would be inappropriate. Accordingly, the final regulations amend the investment asset basis reduction rule by providing that, with respect to a partner other than a C corporation or tax-exempt corporation, the partner's adjusted basis in its partnership interest is decreased by the partner's share of the excess of (a) the partnership's asset basis with respect to those assets over (b) the partnership's debt that is traced to such assets in accordance with § 1.163–8T. In order to neutralize the effect of any cost recovery deductions associated with a partnership's investment assets funded by partnership liabilities (for example, non-trade or business property held for the production of income), the final regulations also amend the investment asset basis reduction rule by providing that, with respect to a partner other than a C corporation or tax-exempt corporation, the partner's adjusted basis in its partnership interest is increased by the partner's share of the excess of (a) the partnership's debt that is traced to such assets in accordance with § 1.163–8T over (b) the partnership's asset basis with respect to those assets.

vi. Allocating Basis in a Partnership Interest Between Excepted and Non-Excepted Trades or Businesses

A commenter requested explicit confirmation that, under the look-through rule, a partner allocates the basis of its partnership interest between excepted and non-excepted trades or businesses in the same proportion as the partner's share of the partnership's adjusted tax basis in its trade or business assets is allocated between excepted and non-excepted trades or businesses. The final regulations explicitly state that this is the rule.

Commenters also stated that the proposed regulations do not address how a partner should allocate business interest expense and business interest income under proposed § 1.163(j)–10(c) to the extent the partner (i) has zero basis in all partnership interests for purposes of section 163(j), and (ii) owns no other trade or business assets. The Treasury Department and the IRS have determined that these facts would be rare, particularly given the adjustments to partnership basis provided for in § 1.163(j)–10. Therefore, the final regulations do not include a rule addressing this fact pattern. However, the Treasury Department and the IRS request comments on how frequently this fact pattern would occur and how best to address such a situation.

3. Additional Limitation on Application of Look-Through Rules to C Corporations

A commenter noted that the look-through rules may be distortive if an individual (A) that is directly engaged in a trade or business also owns stock in a C corporation (with its own trade or business) that satisfies the section 1504(a)(2) ownership requirements. A's interest expense that is attributable to A's investment in the C corporation under § 1.163–8T retains its character as investment interest expense. Moreover, if A also has business interest expense, the allocation of that expense between excepted and non-excepted trades or businesses would appear to take into account A's investment in the C corporation on a look-through basis as well. Thus, A's shares in the C corporation may be double-counted insofar as they affect the character of both the directly attributable investment interest expense and the unrelated business interest expense.

To address the possible distortive effects of the look-through rules when applied to stock of a non-consolidated C corporation that is held as an investment, the final regulations provide that the look-through rule in § 1.163(j)–10(c)(5)(ii)(B)(*2*)(*i*) is available only if dividends paid on the stock would not be included in the taxpayer's investment income under section 163(d)(4)(B). Because corporations cannot have investment income under section 163(d)(4)(B), this additional requirement does not otherwise affect their ability to look-through the stock of a non-consolidated C corporation.

4. Dispositions of Stock in Non-Consolidated C Corporations

Under proposed § 1.163(j)–10(b)(4)(i), if a shareholder recognizes gain or loss upon the disposition of its stock in a non-consolidated C corporation, if such stock is not property held for investment, and if the taxpayer looks through to the assets of the C corporation under proposed § 1.163(j)–10(c)(5)(ii)(B), then the taxpayer must allocate gain or loss from the stock disposition to excepted or non-excepted trades or businesses based upon the relative amounts of the corporation's adjusted basis in the assets used in its trades or businesses. This rule is analogous to the look-through rule for dividends in proposed § 1.163(j)–10(b)(3).

However, the dividend look-through rule also provides that, if at least 90 percent of the payor corporation's adjusted basis in its assets during the taxable year is allocable to either excepted or non-excepted trades or businesses, then all of the taxpayer's dividend income from the payor corporation for the taxable year is treated as allocable to excepted or non-excepted trades or businesses, respectively. Commenters asked why the rule regarding the disposition of non-consolidated C corporation stock is not subject to a 90 percent de minimis rule analogous to the rule for dividends.

The Treasury Department and the IRS have determined that the rule regarding the disposition of stock in a non-consolidated C corporation (including a CFC) should be subject to a 90 percent de minimis rule. The final regulations have modified proposed § 1.163(j)–10(b)(4)(i) accordingly.

5. Application of Look-Through Rules to Small Businesses

Under proposed § 1.163(j)–10(c)(5)(ii)(D), a taxpayer may not apply the look-through rules in proposed § 1.163(j)–10(b)(3) and (c)(5)(ii)(A), (B), and (C) to an entity that is eligible for the small business exemption. As described in the preamble to the proposed regulations, the Treasury Department and the IRS determined that these look-through rules should not be available in these cases because of the administrative burden that would be imposed on small businesses from collecting and providing information to their shareholders or partners regarding inside asset basis when those small businesses are themselves exempt from the application of section 163(j). The preamble to the proposed regulations also provides that a taxpayer that is eligible for the small business exemption may not make an election under proposed § 1.163(j)–9.

Commenters requested that entities that qualify for the small business exemption be allowed to make an election under proposed § 1.163(j)–9, and that such an electing entity's shareholders or partners be permitted to apply the look-through rules. Absent such a rule, shareholders and partners of a small business entity that conducts an excepted trade or business could be worse off than shareholders and partners of a larger entity (ineligible for the small business exemption) that conducts an excepted trade or business.

As noted in part X(A) of this Summary of Comments and Explanation of Revisions section, the Treasury Department and the IRS have determined that entities eligible for the small business exemption should be permitted to make a protective election under proposed § 1.163(j)–9. Accordingly, the final regulations also allow taxpayers to apply the look-through rules to entities that qualify for the small business exemption and that make a protective election under proposed § 1.163(j)–9.

6. Application of the Look-Through Rules to Foreign Utilities

Section 163(j)(7)(A)(iv) does not treat utilities that are exclusively regulated by foreign regulators (and not by a State government, a political subdivision of a State government, an agency or instrumentality of the United States, or the governing or ratemaking body of a domestic electric cooperative) (foreign-regulated utility) as excepted trades or businesses. As a result, under the interest allocation rules of proposed § 1.163(j)–10(c), a U.S. corporation that looks through to the assets of a CFC that operates a foreign-regulated utility must allocate its entire basis in its CFC stock to a non-excepted trade or business, even if all of the CFC's operating assets are used in a foreign-regulated utility business. Moreover, if the U.S. corporation has significant basis in its CFC stock, a significant portion of the U.S. corporation's business interest expense will be subject to the section

163(j) limitation, even if the U.S. corporation is solely or primarily engaged in an excepted utility trade or business.

A commenter noted that, if the U.S. corporation does not have sufficient income from non-excepted trades or businesses, the corporation might never be able to deduct its disallowed business interest expense. The commenter thus recommended that stock in a CFC engaged in a foreign-regulated utility trade or business be treated as having zero basis for purposes of the interest allocation rules in proposed § 1.163(j)–10(c).

The final regulations do not adopt the commenter's recommendation. However, the Treasury Department and the IRS have determined that, if a taxpayer applies the look-through rule to a CFC, the taxpayer may allocate its basis in its CFC stock to an excepted trade or business to the extent the CFC is engaged in either (i) an excepted trade or business, or (ii) a foreign-regulated utility trade or business that would be treated as an excepted trade or business if the utility meets certain requirements related to regulation by a foreign government. The final regulations have been modified accordingly. See § 1.163(j)–10(c)(5)(ii)(C)(*2*).

I. Deemed Asset Sale

Proposed § 1.163(j)–10(c)(5)(iv) provides that, solely for purposes of determining the amount of basis allocable to excepted and non-excepted trades or businesses under proposed § 1.163(j)–10(c), an election under section 336, 338, or 754, as applicable, is deemed to have been made for any acquisition of corporate stock or partnership interests with respect to which the taxpayer demonstrates to the satisfaction of the Commissioner that the taxpayer was eligible to make an election but was actually or effectively precluded from doing so by a regulatory agency with respect to an excepted regulated utility trade or business. As explained in the preamble to the proposed regulations, this deemed asset sale rule is intended to place taxpayers that are actually or effectively precluded from making an election under section 336, section 338, or section 754 on the same footing for purposes of the basis allocation rules in proposed § 1.163(j)–10(c) as taxpayers that are not subject to such limitations.

Commenters pointed out that, as a practical matter, a basis step-up election generally cannot be made if the acquired entity has a regulatory liability for deferred taxes on its books because, in that case, the election may cause customer bills to increase. In other words, deferred tax liabilities typically lower a utility's rate base (which is used to compute the rates charged to customers). An election under section 336, section 338, or section 754 would eliminate this deferred tax liability, thereby increasing the rate base and potentially increasing the rates charged to customers. As a result, regulatory agencies frequently do not approve a basis step-up election made in connection with the sale or purchase of a regulated utility. Commenters argued that even broaching the possibility of such a basis step-up could create concerns for the regulatory agency regarding a proposed acquisition. Commenters also queried how taxpayers that do not raise this issue with the regulatory agency can ''demonstrate'' that they were ''effectively precluded'' by the agency from making the election. In short, commenters claimed that the ''demonstration'' requirement in proposed § 1.163(j)–10(c)(5)(iv) would be impractical, result in unnecessary requests to regulatory agencies, lead to controversy, create uncertainty, and limit the effectiveness of this provision.

To address the foregoing concerns, the final regulations provide that a taxpayer that acquired or acquires an interest in a regulated entity should be deemed to have made an election to step up the tax basis of the assets of the acquired entity if the taxpayer can demonstrate that (a) the acquisition qualified for an election under section 336, 338, or 754, and (b) immediately before the acquisition, the acquired entity had a regulatory liability for deferred taxes on its books with respect to property predominantly used in an excepted regulated utility trade or business.

J. Carryforwards of Disallowed Disqualified Interest

Proposed § 1.163(j)–1(b)(10) defines the term ''disallowed disqualified interest'' to mean interest expense, including carryforwards, for which a deduction was disallowed under old section 163(j) in the taxpayer's last taxable year beginning before January 1, 2018, and that was carried forward under old section 163(j). Under the proposed regulations, disallowed disqualified interest that is properly allocable to a non-excepted trade or business is subject to the section 163(j) limitation as a disallowed business interest expense carryforward. See proposed §§ 1.163(j)–2(c)(1) and 1.163(j)–11(b)(1). In the preamble to the proposed regulations, the Treasury Department and the IRS requested comments as to how the allocation rules in proposed § 1.163(j)–10 should apply to disallowed disqualified interest.

Commenters recommended several possible approaches to allocating disallowed disqualified interest between excepted and non-excepted trades or businesses. Under one approach (historical approach), a taxpayer would apply the allocation rules of proposed § 1.163(j)–10 to disallowed disqualified interest in the taxable year in which such interest expense was incurred. Although this approach would be consistent with the allocation rules for other business interest expense, it likely would be administratively burdensome for many taxpayers because such interest expense may have been incurred years (if not decades) ago.

Under another approach (effective date approach), a taxpayer would apply the allocation rules of proposed § 1.163(j)–10 to disallowed disqualified interest in the taxpayer's first taxable year beginning after December 31, 2017, as if the disallowed disqualified interest expense were incurred in that year. Although this approach would be less administratively burdensome than the historical approach, it might not accurately represent the taxpayer's circumstances in the year(s) in which the disallowed disqualified interest actually was incurred.

Under a third approach, taxpayers would be permitted to use any reasonable method to allocate disallowed disqualified interest between excepted and non-excepted trades or businesses, provided the method is applied consistently to disallowed disqualified interest that arose in the same taxable year. This approach also might include the effective date approach as a safe harbor. However, this approach could prove to be administratively burdensome for the IRS.

To reduce the administrative burden for both taxpayers and the IRS, the final regulations permit taxpayers to use either the historical approach or the effective date approach.

A commenter also pointed out that proposed § 1.163(j)–11(b)(1) could be construed as permitting only disallowed disqualified interest that is properly allocable to a non-excepted trade or business to be carried forward to the taxpayer's first taxable year beginning after December 31, 2017. The commenter requested confirmation that disallowed disqualified interest that is properly allocable to an excepted trade or business also is carried forward. The final regulations confirm this point. See § 1.163(j)–11(c)(1).

K. Anti-Abuse Rule

Proposed § 1.163(j)–10(c)(8) provides an anti-abuse rule to discourage taxpayers from manipulating the allocation of business interest expense and business interest income between non-excepted and excepted trades or businesses. Pursuant to this provision, if a principal purpose for the acquisition, disposition, or change in use of an asset was to artificially shift the amount of basis allocable to excepted or non-excepted trades or businesses on a determination date, the additional basis or change in use is not taken into account for purposes of § 1.163(j)–10.

A commenter expressed support for this rule but suggested that the final regulations eliminate the ''principal purpose'' standard and rely instead on a rule based on asset acquisitions, dispositions, or changes in use that do not have ''a substantial business purpose.''

The Treasury Department and the IRS have determined that using ''a substantial business purpose'' as the threshold for applying the anti-abuse rule would limit the effectiveness of this rule because taxpayers generally would be able to provide an ostensible business purpose for the acquisition, disposition, or transfer of an asset. Thus, the anti-abuse rule in the final regulations retains the ''principal purpose'' standard.

L. Direct Allocation

1. Overview

As previously noted, proposed § 1.163(j)–10(c) generally requires interest expense and interest income to be allocated between excepted and non-excepted trades or businesses according to the relative amounts of basis in the assets used in such trades or businesses. However, proposed § 1.163(j)–10(d) contains several exceptions to this general rule.

First, a taxpayer with qualified nonrecourse indebtedness is required to directly allocate interest expense from such indebtedness to the taxpayer's assets in the manner and to the extent provided in § 1.861–10T(b) (see proposed § 1.163(j)–10(d)(1)). Section 1.861–10T(b) defines the term ''qualified nonrecourse indebtedness'' to mean any borrowing (other than borrowings excluded by § 1.861–10T(b)(4)) that satisfies certain requirements, including the requirements that (i) the creditor can look only to the identified property (or any lease or other interest therein) as security for payment of the principal and interest on the loan, and (ii) the cash flow from the property is reasonably expected to be sufficient to fulfill the terms and conditions of the loan agreement. For these purposes, the term ''cash flow from the property'' does not include revenue if a significant portion thereof is derived from activities such as sales or the use of other property. Thus, revenue derived from the sale or lease of inventory or similar property, including plant or equipment used in the manufacture and sale or lease, or purchase and sale or lease, of such inventory or similar property, does not constitute cash flow from the property. See § 1.861–10T(b)(3)(i).

Second, a taxpayer that is engaged in the trade or business of banking, insurance, financing, or a similar business is required to directly allocate interest expense and interest income from such business to the taxpayer's assets used in that business (see proposed § 1.163(j)–10(d)(2)).

Additionally, for purposes of the general allocation rule in proposed § 1.163(j)–10(c), taxpayers are required to reduce their asset basis by the entire amount of the basis in the assets to which interest expense is directly allocated pursuant to proposed § 1.163(j)–10(d)(1) or (2). See proposed § 1.163(j)–10(d)(4).

2. Expansion of the Direct Allocation Rule

Some commenters recommended that the direct allocation rule in proposed § 1.163(j)–10(d) be applied in circumstances other than those set forth in proposed § 1.163(j)–10(d)(1) and (2). For example, a commenter queried whether a borrowing could be considered qualified nonrecourse indebtedness for purposes of proposed § 1.163(j)–10(d) even if the loan document doesn't require the creditor to look exclusively to an asset as security for payment of principal and interest on a loan (as required by § 1.861–10T(b)(2)(iii)). Other commenters asked that direct allocation be applied to debt directly incurred by an excepted regulated utility trade or business. These commenters argued that, because such debt must be approved by a regulatory agency and relates directly to the underlying needs of that trade or business, such debt should be viewed as ''properly allocable'' to that trade or business. Moreover, they claimed that the definition of ''qualified nonrecourse indebtedness'' in § 1.861–10T(b) is too narrow to include either debt directly incurred by an excepted regulated utility trade or business or debt incurred to purchase stock of a corporation or interests in a partnership primarily engaged in an excepted regulated utility trade or business.

In contrast, other commenters supported the decision to limit the availability of tracing to the limited circumstances in proposed § 1.163(j)–10(d).

As noted in part XI(L)(1) of this Summary of Comments and Explanation of Revisions section, a borrowing is not considered qualified nonrecourse indebtedness under § 1.861–10T(b) unless the creditor can look only to the identified property (or any interest therein) as security for the loan. By definition, the creditor on a non-recourse loan may not seek to recover the borrower's other assets; in other words, the creditor has no further recourse. The Treasury Department and the IRS decline to expand the exception in proposed § 1.163(j)–10(d)(1) to include unsecured debt because, by definition, such debt is supported by all of the assets of the borrower.

The Treasury Department and the IRS also have determined that the definition of qualified nonrecourse indebtedness should not be expanded to encompass indebtedness incurred to acquire stock or partnership interests in an entity primarily engaged in an excepted trade or business because such an approach is akin to tracing. As noted in the preamble to the proposed regulations, money is fungible, and the Treasury Department and the IRS have determined that a tracing regime would be inappropriate, with limited exceptions. The Treasury Department and the IRS have determined that the definition of qualified nonrecourse indebtedness should not be expanded to encompass all indebtedness directly incurred by regulated utility trades or businesses, for similar reasons.

However, the Treasury Department and the IRS appreciate that it is difficult for utility trades or businesses to avail themselves of the direct allocation rule in proposed § 1.163(j)–10(d)(1) given the definition of qualified nonrecourse debt in § 1.861–10T(b). In particular, the Treasury Department and the IRS understand that the exclusion of inventory revenue from the calculation of ''cash flow from the property'' effectively precludes many utilities from using direct allocation under proposed § 1.163(j)–10(d)(1). Thus, solely for purposes of the allocation rules in proposed § 1.163(j)–10, the final regulations create an exception to the definition of qualified nonrecourse indebtedness in § 1.861–10T(b) to allow for the inclusion of revenue from the sale or lease of inventory for utility trades or businesses.

Another commenter recommended that, for taxpayers engaged in excepted regulated utility trades or businesses, the basis in certain grants and contributions in aid of construction should be directly allocated to non-excepted trades or businesses if the costs have not been taken into account by a regulatory body in determining the cost of the utility's service for ratemaking purposes. As discussed in part II of this Summary of Comments and Explanation of Revisions section, the final regulations do not require the rates for the sale or furnishing of utility items to be established or approved on a cost of service and rate of return basis in order for a utility trade or business to qualify as an excepted regulated utility trade or business. Without such a requirement, the Treasury Department and the IRS do not find a significant nexus between a regulatory body's determination of a utility trade or business's cost of service and the allocation of the basis in grants and contributions in aid of construction. Therefore, the final regulations do not adopt the commenter's recommendation.

3. Basis Reduction Requirement for Qualified Nonrecourse Indebtedness

Commenters noted that, as drafted, the basis reduction requirement in proposed § 1.163(j)–10(d)(4) would lead to inappropriate results for assets that are acquired using both equity financing and qualified nonrecourse indebtedness (or using both recourse and nonrecourse indebtedness) because this requirement would remove asset basis that was not financed by qualified nonrecourse indebtedness.

Commenters also observed that this requirement could lead to significant distortions because a small amount of qualified nonrecourse indebtedness would cause an entire property to be removed from a taxpayer's basis allocation computation. For example, assume a taxpayer has (i) $500,000 of unsecured debt, (ii) property used in an excepted trade or business with a basis of $10 million and $100,000 of qualified nonrecourse indebtedness (Asset A), and (iii) a non-excepted trade or business whose assets have a basis of $1 million. Under proposed § 1.163(j)–10(d)(4), Asset A would be entirely excluded from the basis allocation computation in proposed § 1.163(j)–10(c). As a result, all interest expense on the $500,000 of unsecured debt would be subject to the section 163(j) limitation.

Commenters further noted that taxpayers could take advantage of this basis adjustment rule to minimize the application of section 163(j). In other words, taxpayers could incur a relatively small amount of nonrecourse debt to acquire assets used in non-excepted trades or businesses, thereby reducing the amount of asset basis allocated to such trades or businesses for purposes of the general allocation rule in proposed § 1.163(j)–10(c).

To eliminate these distortions and inappropriate results, commenters recommended that basis in the assets securing qualified nonrecourse indebtedness be reduced (but not below zero) for purposes of the general allocation rule solely by the amount of such qualified nonrecourse indebtedness. The Treasury Department and the IRS agree with this recommendation, and the final regulations have been modified accordingly.

4. Direct Allocation Rule for Financial Services Businesses

Commenters asked for clarification of the direct allocation rule for financial services entities in proposed § 1.163(j)–10(d)(2). For example, commenters noted that, because the definition in § 1.904–4(e)(2) includes income from certain services (including investment advisory services), this rule may apply to taxpayers that are not doing much actual financing, and commenters queried whether the direct allocation rule should apply to such taxpayers. Commenters also asked whether proposed § 1.163(j)–10(d)(2) is intended to cover all of a bank's activities or only part of them and, if the answer is the latter, whether a bank must bifurcate its activities for purposes of proposed § 1.163(j)–10.

Commenters also questioned the basis reduction rule in proposed § 1.163(j)–10(d)(4) for financial services businesses. Commenters noted that, unlike the case of qualified nonrecourse indebtedness, it may not be possible to trace all interest expense related to a financial services business to specific assets. Moreover, requiring a taxpayer to fully eliminate its basis in the assets of a financial services business under proposed § 1.163(j)–10(d)(4) could be distortive because the taxpayer's general debt obligations likely support at least some portion of the taxpayer's financial services business assets.

Given the uncertainty surrounding the proper scope of the direct allocation rule for financial services businesses in proposed § 1.163(j)–10(d)(2) and the proper application of the basis reduction rule to such businesses in proposed § 1.163(j)–10(d)(4), the Treasury Department and the IRS have decided to remove proposed § 1.163(j)–10(d)(2). To ensure that financial services entities are not unduly affected by the rule (in proposed § 1.163(j)–10(c)(5)(iii)) that excludes cash and cash equivalents from the general asset basis allocation rule in proposed § 1.163(j)–10(c), the final regulations have retained the exception in proposed § 1.163(j)–10(c)(5)(iii) for financial services entities.

XII. Comments on Proposed Changes to § 1.382–2: General Rules for Ownership Change

As described in the preamble to the proposed regulations, section 382(k)(1) provides that, for purposes of section 382, the term ''loss corporation'' includes a corporation entitled to use a carryforward of disallowed interest described in section 381(c)(20), which refers to carryovers of disallowed business interest described in section 163(j)(2). Section 163(j)(2) permits business interest expense for which a deduction is disallowed under section 163(j)(1) to be carried forward to the succeeding taxable year.

In turn, section 382(d)(3) provides that the term ''pre-change loss'' includes disallowed business interest expense carryforwards ''under rules similar to the rules'' in section 382(d)(1). Section 382(d)(1) treats as a ''pre-change loss'' both (i) net operating loss carryforwards to the taxable year in which the change date occurs (change year), and (ii) the net operating loss carryforward for the change year to the extent such loss is allocable to the pre-change period.

Proposed changes to § 1.382–2 clarified that a ''pre-change loss'' includes the portion of any disallowed business interest expense of the old loss corporation paid or accrued in the taxable year of the testing date that is attributable to the pre-change period, and that a ''loss corporation'' includes a corporation that is entitled to use a carryforward of such a disallowed business interest expense.

Commenters noted that, viewed in isolation, section 382(k)(1) would not appear to apply to a corporation that has only a current-year disallowed business interest expense. Some commenters also claimed that the inclusion of current-year disallowed business interest expense in the definition of a ''loss corporation'' is inconsistent with the statutory language of section 382(k)(1).

The Treasury Department and the IRS have determined that section 382 should apply to current-year disallowed business interest expense (to the extent such expense is allocable to the pre-change period) because this approach is consistent with the statutory treatment of NOLs. See section 382(k)(1) (providing, in part, that the term ''loss corporation'' means a corporation ''having a net operating loss for the taxable year in which the ownership change occurs''). Moreover, as a policy matter, current-year attributes that relate to the period before an ownership change should be subject to section 382. The exclusion of these items would permit trafficking in losses, which is contrary to the stated policy underlying section 382 of preventing ''exploit[ation] by persons other than those who incurred the loss.'' H. Rept. 83–1337, at 42 (1954). Thus, no changes to the final regulations have been made in response to these comments. However, the final regulations revise the definition of a ''section 382 disallowed business interest carryforward'' (which includes both disallowed business interest expense carryforwards and current-year disallowed business interest expense allocable to the pre-change period) in § 1.382–2(a)(7) to reflect changes to the allocation rules discussed in part XIII of this Summary of Comments and Explanation of Revisions section.

XIII. Comments on Proposed Changes to § 1.382–6: Allocation of Income and Loss to Periods Before and After the Change Date for Purposes of Section 382

Section 1.382–6 provides rules for the allocation of income and loss to periods before and after the change date for purposes of section 382. Section 1.382–6(a) generally provides that a loss corporation must allocate its net operating loss or taxable income, and its net capital loss or modified capital gain net income, for the change year between the pre-change and post-change periods by ratably allocating an equal portion to each day in the year. Section 1.382–6(b), which contains an exception to this general rule, permits a loss corporation to elect to allocate the foregoing items for the change year between the pre-change and post-change periods as if the loss corporation's books were closed on the change date. Such an election does not terminate the loss corporation's taxable year as of the change date (in other words, the change year is still treated as a single tax year for Federal income tax purposes).

The proposed regulations revise § 1.382–6 to address the treatment of business interest expense. More specifically, the proposed regulations provide that, regardless of whether a loss corporation has made a closing-of-the-books election under § 1.382–6(b), the amount of the corporation's deduction for current-year business interest expense is calculated based on ratable allocation for purposes of calculating the corporation's taxable income attributable to the pre-change period.

Commenters objected to the mandatory use of ratable allocation for business interest expense in § 1.382–6. For example, commenters argued that this approach is distortive (and taxpayer-unfavorable) in situations in which the loss corporation incurs minimal interest expense in the pre-change period but makes highly leveraged acquisitions in the post-change period. Another commenter noted that this approach is distortive (and taxpayer-favorable) in situations in which the loss corporation incurs significant business interest expense in the pre-change period and allocates a portion of that expense to the post-change period. To avoid these distortions and complications, commenters recommended that a closing-of-the-books election also be allowed for business interest expense.

The Treasury Department and the IRS acknowledge that a ratable allocation approach may lead to distortions and administrative burdens in certain situations. Thus, the final regulations permit a loss corporation to allocate current-year business interest expense between the pre-change and post-change periods using the closing-of-the-books method set forth in § 1.382–6(b)(4) if the loss corporation makes a closing-of-the-books election under § 1.382–6(b). Section 1.382–6(b)(4) also provides correlative rules for the allocation of disallowed business interest expense carryforwards to the pre-change and post-change periods when a closing-of-the-books election is made. In turn, section 1.382–6(a)(2) clarifies the amount of business interest expense, disallowed business interest expense, and disallowed business interest expense carryforwards that are allocable to the pre-change and post-change periods if no closing-of-the-books election is made.

XIV. Comments on and Changes to Proposed § 1.383–1: Special Limitations on Certain Capital Losses and Excess Credits

Section 1.383–1(d) provides ordering rules for the utilization of pre-change losses and pre-change credits and for the absorption of the section 382 limitation and the section 383 credit limitation. Under proposed changes to § 1.383–1(d), a taxpayer's section 382 limitation would be absorbed by disallowed business interest expense carryforwards before being absorbed by NOLs. As described in the preamble to the proposed regulations, the Treasury Department and the IRS prioritized the use of disallowed business interest expense carryforwards over NOLs because ''taxpayers must calculate their current-year income or loss in order to determine whether and to what extent they can use an NOL in that year, and deductions for business interest expense, including carryforwards from prior taxable years, factor into the calculation of current-year income or loss.''

Although commenters described the foregoing ordering rule as understandable and fairly simple to administer, they noted that pre-2018 NOLs (unlike disallowed business interest expense carryforwards) have a limited carryforward period, and that such NOLs may expire without use as a result of this ordering rule. Commenters thus recommended allowing taxpayers to elect an alternative ordering rule with respect to pre-2018 NOLs.

The Treasury Department and the IRS have decided not to adopt this recommended approach, for several reasons. First, as commenters also noted, such an approach would add complexity. Second, as stated in the preamble to the proposed regulations, deductions for business interest expense (including disallowed business interest expense carryforwards) factor into the determination whether and to what extent a taxpayer can use an NOL in a taxable year. Thus, no changes have been made to proposed § 1.383–1(d) in the final regulations.

XV. Other Comments About Section 382

A. Application of Section 382(l)(5)

Section 382(l)(5) provides an exception to the general loss limitation rule under section 382(a) for an old loss corporation in Title 11 proceedings or in similar cases if the historic shareholders and creditors of such corporation own at least 50 percent of the stock of the new loss corporation as a result of being shareholders or creditors immediately before the ownership change. If this exception applies, the corporation's pre-change losses and excess credits that may be carried over to a post-change year must be ''computed as if no deduction was allowable under this chapter for the interest paid or accrued'' on debt converted into stock under Title 11 (or in a similar case) during the 3-year period preceding the year of the ownership change (change year) or during the pre-change period in the change year. Section 382(l)(5)(B). In other words, because the old loss corporation gets the benefit of treating certain creditors as shareholders for purposes of determining whether the corporation has undergone an ownership change within the meaning of section 382(g), the corporation must treat the debt held by such creditors as equity for Federal income tax purposes. As a result, the corporation must treat the interest payments as non-deductible distributions on equity.

As provided in proposed § 1.382–2, section 382 disallowed business interest carryforwards are pre-change losses. Because a deduction for such carryforwards is ''allowable'' in a future year, commenters asked whether such carryforwards must be recomputed under section 382(l)(5)(B).

The Treasury Department and the IRS have determined that no clarification of the rule is necessary. Because section 382 disallowed business interest carryforwards are pre-change losses, if a corporation has such a carryforward from any taxable year ending during the 3-year period preceding the change year (or during the pre-change period in the change year), and if section 382(l)(5) applies to an ownership change, the corporation must recompute the amount of such carryforwards as if the business interest expense that generated such carryforwards were not interest.

B. Application of Section 382(e)(3)

A commenter also recommended that the final regulations address the application of section 382(e)(3) to foreign corporations with section 382 disallowed business interest carryforwards. Section 382(e)(3) provides that, except as otherwise provided in regulations, only items treated as connected with the conduct of a U.S. trade or business are taken into account in determining the value of an old loss corporation that is a foreign corporation if an ownership change occurs. Thus, if a foreign corporation is not engaged in a U.S. trade or business, that corporation's section 382 limitation is zero. As a result, if a foreign corporation with no U.S. trade or business undergoes a section 382 ownership change, section 382(e)(3) appears to limit the corporation's section 382 disallowed business interest carryforwards to $0. The commenter described this result as onerous and unintended and recommended that, for purposes of applying section 382 to such carryforwards, a foreign corporation's value be treated as the total value of its stock.

The Treasury Department and the IRS are aware of this issue and other issues relating to the application of section 382 to CFCs. The Treasury Department and the IRS continue to study the application of section 382 to CFCs and may address this issue in future guidance. The Treasury Department and the IRS welcome further comments on the application of section 382 to CFCs.

C. Application of Section 382(h)(6)

As noted in the Background section, the September 2019 section 382 proposed regulations included a rule expressly providing that section 382 disallowed business interest carryforwards are not treated as RBILs, thus precluding a double detriment under section 382 with respect to such carryforwards. This conclusion might have been reached by application of the general anti-duplication principles reflected in the current regulations under section 382. See, for example, § 1.382–8(d) (regarding duplicative reductions in value of loss corporations). However, because of the complexity of this area, the Treasury Department and the IRS included the clarification to prevent possible confusion and to provide certainty to taxpayers that there is no double detriment with respect to section 382 disallowed business interest carryforwards. Although no formal comments were received on this rule during the comment period for the September 2019 section 382 proposed regulations, informal comments from practitioners active in the field have been uniformly positive and have confirmed that this rule is a welcome, taxpayer-beneficial addition to the regulations under section 382.

Due to the uncontroversial nature of this rule, the Treasury Department and the IRS have determined that finalization of this portion of the September 2019 section 382 proposed regulations is warranted at this time. The Treasury Department and the IRS continue to actively study the remainder of the rules in the September 2019 section 382 proposed regulations.

XVI. Definition of Real Property Trade or Business

Commenters suggested that the definition of a ''real property trade or business'' should be clarified to include all rental real estate, even if the rental real estate does not rise to the level of a section 162 trade or business. The Treasury Department and the IRS have determined that modifications to the rules in the proposed regulations are not necessary to make this point clear. Section 1.469–9(b)(1) provides that the definition of a ''trade or business'' (for purposes of section 469(c)(7)(C)) includes interests in rental real estate even if the rental real estate gives rise to deductions under section 212. The definition of real property trade or business in § 1.469–9(b)(2) (for purposes of section 469(c)(7)(C)) necessarily would encompass or include the definition of a trade or business as provided in § 1.469–9(b)(1). Accordingly, taxpayers engaged in rental real estate activities that do not necessarily rise to the level of a section 162 trade or business nevertheless will be treated as engaged in real property trades or businesses for purposes of section 469(c)(7)(C) (and section 163(j) by reference), and such taxpayers will be permitted to make the election for a trade or business to be an electing real property trade or business for purposes of section 163(j).

Commenters also requested clarification that a trade or business should not be required to have a direct nexus or relationship to rental real estate in order to qualify as a real property trade or business under section 469(c)(7)(C). The Treasury Department and the IRS agree that businesses involving real property construction, reconstruction, development, redevelopment, conversion, acquisition, or brokerage should not necessarily be required to have a direct nexus or relationship to rental real estate to be treated as a real property trade or business under section 469(c)(7)(C). The proposed regulations provide definitions for the terms ''real property management'' and ''real property operations'' while reserving the remaining nine terms in section 469(c)(7)(C) as undefined. The statement in the preamble to the proposed regulations regarding a nexus or relationship to rental real estate was intended as the rationale for the decision to limit the definition of the two terms to the management and operation of rental real estate. Without these limiting definitions, the Treasury Department and the IRS were concerned that these two terms could be read so broadly as to allow virtually any type of business to qualify as a real property trade or business. The other nine terms in section 469(c)(7)(C) currently remain undefined, although the Treasury Department and the IRS intend to issue additional guidance in the future to provide definitions for these terms.

The Treasury Department and the IRS generally agree with the observation that real property construction, reconstruction, development, redevelopment, conversion, acquisition, or brokerage businesses should not necessarily be required to have a direct nexus or relationship to rental real estate in order to be treated as real property trades or businesses. However, the expectation nevertheless remains that the end products or final objectives of such businesses should at least have the potential to be used as rental real estate or as integral components in rental real estate activities.

Several commenters requested clarification regarding whether timberlands will qualify as real property trades or businesses. The Treasury Department and the IRS have concluded that unharvested or unsevered timber clearly fall within the definition of ''real property'' as provided in the proposed regulations. The question is whether the activity of holding of timberlands falls within the definition of a ''real property trade or business.'' The Treasury Department and the IRS have concluded that the maintenance and management of timberlands generally does not meet the intended meaning of any of the eleven terms in section 469(c)(7)(C), and that the owners of timberlands were not intended recipients for relief from the per se passive rule for rental real estate when section 469(c)(7) originally was enacted. However, as set forth in the Concurrent NPRM, such activities might constitute the development of real estate within the meaning of section 469(c)(7)(C). See proposed § 1.469–9(b)(2)(ii)(A) and (B) contained in the Concurrent NPRM.

One commenter requested an example illustrating that the management or operation of a pipeline or transmission line will meet the definition of a real property trade or business. In addition, another commenter requested an example illustrating that the operation of a bridge, tunnel, toll road, or airport qualifies as a real property trade or business.

Although the Treasury Department and the IRS generally agree that the operation of a pipeline, bridge, tunnel, toll road, or airport may meet the definition of a real property trade or business under certain and specific facts and circumstances, the answers to these questions will remain dependent on the facts and circumstances of each case. The Treasury Department and the IRS expect that such examples generally will provide very limited guidance to most taxpayers because any such examples likely will be viewed as inapplicable for taxpayers with any differing facts and circumstances.

Additionally, one commenter recommended removing the reference to the term ''customers'' from the definitions of the terms ''real property management'' and ''real property operation'' because, in certain situations, the party paying for the use of the property or for other services may be a governmental agency providing services to the general public or for the public good. The Treasury Department and the IRS have determined that this modification is unnecessary because the term ''customer'' for this purpose is broad enough to include governmental entities.

One commenter also requested that the definition of a real property trade or business be revised to include broadband, street lighting, telephone poles, parking meters, and rolling stock. The Treasury Department and the IRS decline to revise the definition of real property trade or business in section 469(c)(7)(C) in this manner because the maintenance and management of these types of assets generally do not meet the intended meaning of any of the eleven terms in section 469(c)(7)(C), and the owners of such assets were not intended recipients for relief from the per se passive rule for rental real estate when section 469(c)(7) originally was enacted.

One commenter requested that the final regulations remove the last sentence in the definition of each of the terms ''real property management'' and ''real property operation.'' The commenter stated that these sentences create confusion regarding whether incidental services provided along with rental real estate will cause the business to fail to qualify as a real property trade or business. In response to this comment, the Treasury Department and the IRS have revised these sentences to clarify that incidental services, even if significant, do not disqualify a business as a real property trade or business.

Statement of Availability of IRS Documents

The IRS Notices, Revenue Rulings, and Revenue Procedures cited in this document 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.*

Special Analyses

I. Regulatory Planning and Review—Economic Analysis

Executive Orders 13771, 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.

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. OMB has designated this final regulation as economically significant under section 1(c) of the Memorandum of Agreement. Accordingly, the final regulations have been reviewed by OMB's Office of Information and Regulatory Affairs. For purposes of E.O. 13771 this rule is regulatory.

A. Need for the Final Regulations

The Tax Cuts and Jobs Act (TCJA) substantially modified the statutory rules of section 163(j) to limit the amount of net business interest expense that can be deducted in the current taxable year. As a result of those changes, a number of the relevant terms and necessary calculations that taxpayers are required to apply under the statute can benefit from greater specificity. The Treasury Department and the IRS issued proposed regulations related to section 163(j) on December 28, 2018 (proposed regulations). The comments to the proposed regulations demonstrate a variety of opinions on how to define terms and on how section 163(j) interacts with other sections of the Code and corresponding regulations.

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. Among other benefits, the clarity provided by the final regulations generally helps ensure that all taxpayers calculate the business interest expense limitation in a similar manner.

B. Background and Overview

The TCJA substantially modified the statutory rules of section 163(j) to limit the amount of net business interest expense that can be deducted in the current taxable year of any taxpayer, with limited exceptions. As described in the preamble to the proposed regulations (83 FR 67490), section 163(j) prior to TCJA generally applied to domestic corporations with interest paid or accrued to related persons that were not subject to Federal income tax. With the enactment of TCJA, the amount allowed under section 163(j)(1) as a deduction for business interest expense is limited to the sum of (1) the taxpayer's business interest income for the taxable year; (2) 30 percent of the taxpayer's adjusted taxable income (ATI) for the taxable year; and (3) the taxpayer's floor plan financing interest expense for the taxable year. As described in the Background section earlier, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) amended section 163(j) to provide special rules relating to the ATI limitation for taxable years beginning in 2019 or 2020. The section 163(j) limitation applies to all taxpayers, except for certain small businesses with average annual gross receipts of $25 million or less (adjusted for inflation) and certain trades or businesses. The excepted trades or businesses are the trade or business of providing services as an employee, electing real property businesses, electing farming businesses, and certain regulated utility businesses. Any amount of business interest not allowed as a deduction for any taxable year as a result of the limitation under section 163(j)(1) is carried forward and treated as business interest paid or accrued in the next taxable year under section 163(j)(2).

Congress modified section 163(j) under the TCJA, in part, out of concern that prior law treated debt-financed investment more favorably than equity-financed investment. According to Congress, this debt bias generally encouraged taxpayers to utilize more leverage than they would in the absence of the Code. Limiting the deduction of business interest is meant to reduce the relative favorability of debt and hence encourage a more efficient capital structure for firms. Congress also believed it necessary to apply the limit broadly across different types of taxpayers so as not to distort the choice of entity (see H.R. Rep. No. 115–409, at 247 (2017)).

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 terms and calculations that are contained in section 163(j), which was substantially modified by TCJA. In the absence of this clarity, the likelihood that different taxpayers would interpret the rules regarding the deductibility of business interest expense differently would be exacerbated. In general, overall economic performance is enhanced when businesses face more uniform signals about tax treatment. Certainty and clarity over tax treatment also reduce compliance costs for taxpayers. For those situations where taxpayers would generally adopt similar interpretations of the statute even in the absence of guidance, the final regulations provide value by helping to ensure that those interpretations are consistent with the intent and purpose of the statute. For example, the final regulations may specify a tax treatment that few or no taxpayers would adopt in the absence of specific guidance but that nonetheless advances Congressional intent.

The Treasury Department and the IRS project that the final regulations will have an annual economic effect greater than $100 million ($2020). This determination is based on the substantial volume of business interest payments in the economy [2] and the general responsiveness of business investment to effective tax rates,[3] one component of which is the deductibility of interest expense. Based on these two magnitudes, even modest changes in the deductibility of interest payments (and in the certainty of that deductibility) provided by the final regulations, relative to the no-action baseline, can be expected to have annual effects greater than $100 million. This claim is particularly likely to hold for the first set of general 163(j) guidance that is promulgated following major legislation, such as TCJA.

The Treasury Department and the IRS have not undertaken more precise estimates of the economic effects of changes in business activity stemming from these final regulations. 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 those 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.

In the absence of such quantitative estimates, the Treasury Department and the IRS have undertaken a qualitative analysis of the economic effects of the final regulations relative to the no-action baseline and relative to alternative regulatory approaches. This analysis is presented in the next two sections of this Special Analyses.

3. Economic Effects of Provisions Substantially Revised From the Proposed Regulations

a. Calculation of ATI

Similar to the proposed regulations, the final regulations prescribe various adjustments to the calculation of ATI to prevent double counting of deductions and to provide relief for particular types of taxpayers or taxpayers in particular circumstances to ensure that all taxpayers are treated equitably when calculating ATI. One of these adjustments prevents the double counting of depreciation deductions when a depreciable asset is sold (only relevant for depreciation deductions in taxable years beginning after December 31, 2017, and before January 1, 2022). Other adjustments apply to particular types of taxpayers, such as regulated investment companies (RICs), real estate investment trusts (REITs), or consolidated groups.

As an alternative, the Treasury Department and the IRS considered not providing such adjustments. Without such adjustments, however, certain taxpayers may be disadvantaged relative to otherwise similar taxpayers. For example, if RICs and REITs included the dividends paid deduction when calculating ATI, then these entities would almost always have ATI of zero or close to zero. This outcome would limit the ability of such taxpayers to ever deduct business interest expense for Federal income tax purposes even when their financing profile was similar to other entities that could deduct similar net business interest expense.

Based on calculations using the IRS's Statistics of Income (SOI) sample of corporate taxpayers for 2017, the Treasury Department and the IRS estimate that approximately $13.5 billion of net business interest expense is potentially affected by the dividends paid deduction adjustment to ATI provided to RICs and REITs in the final regulations. This net business interest expense is the amount of interest expense that is greater than interest income for RICs and REITs with gross receipts greater than $25 million.

The final regulations make one notable change compared to the proposed regulations regarding the ATI calculation for taxpayers that manufacture or produce inventory. Under the proposed regulations, the

[2] Interest deductions in tax year 2013 for corporations, partnerships, and sole proprietorships were approximately $800 billion.

[3] See E. Zwick and J. Mahon, ''Tax Policy and Heterogeneous Investment Behavior,'' at *American Economic Review* 2017, 107(1): 217–48 and articles cited therein.

amount of any depreciation, amortization, or depletion that is capitalized into inventory under section 263A during a taxable year beginning before January 1, 2022 was not added back to taxable income when calculating ATI for that taxable year. Under the final regulations, such amounts are added back to tentative taxable income, regardless of the period in which the capitalized amount is recovered through cost of goods sold.

Without the final regulations, a taxpayer with depreciation, amortization, or depletion expense that is subject to capitalization would have lower ATI (and potentially a higher tax liability due to smaller net interest deductions) than a similarly situated taxpayer with depreciation, amortization, or depletion expense that is not subject to capitalization. Thus, the effect of the final regulations for the calculation of ATI is to prevent economic distortions by having the net interest limitation apply more stringently for certain types of taxpayers than others. The final regulations achieve this outcome more effectively that alternative regulatory approaches, including the proposed regulations and the no-action baseline.

Number of Affected Taxpayers. The Treasury Department and the IRS estimate that roughly 61,000 entities are both (i) subject to calculating their section 163(j) net interest limitation and (ii) required by the Code to capitalize any expenses, including depreciation, amortization, or depletion expenses. This estimate is an upper bound estimate of the number of taxpayers potentially affected by the definition of ATI prescribed under the regulations because capitalized depreciation, amortization, or depletion expenses are not separately reported and this tax return item includes other types of capitalized expenses.

b. Definition of Interest

The statute limits the amount of deductible interest expense for a taxpayer but, as described in the Explanation of Provisions section of the proposed regulations, there are no generally applicable statutory provisions or regulations addressing when financial instruments are treated as debt for Federal income tax purposes or when a payment is counted as interest. While there are several places in the Code and regulations where interest expense or interest income is defined, such as in the regulations that allocate and apportion interest expense (§ 1.861–9T) and in the Subpart F regulations (§ 1.954–2), these rules only apply to particular taxpayers in particular situations.

The proposed regulations defined interest for the purpose of the section 163(j) limitation as (1) amounts associated with conventional debt instruments and amounts already treated as interest for all purposes under existing statutory provisions or regulations; (2) additional amounts that are functionally similar to interest but not currently labeled as interest under the Code, or amounts treated as interest for certain purposes, such as amounts described in §§ 1.861–9T and 1.954–2; and (3) any deductible expense or loss predominantly incurred in consideration of the time value of money as part of an anti-avoidance rule. Thus, the proposed regulations applied to interest associated with conventional debt instruments as well as generally to transactions that are indebtedness in substance even if not in form.

The Treasury Department and the IRS proposed this definition of interest, rather than leaving the term interest undefined for purposes of section 163(j). In the absence of this clarity, the likelihood that different taxpayers would reach different conclusions over whether a particular business expense was deductible business interest expense would be exacerbated. In general, overall economic performance is enhanced when businesses face more uniform signals about tax treatment. Another concern about not defining the term at all is that taxpayer uncertainty over whether certain transactions are considered interest could increase burdens to the IRS and taxpayers including with respect to disputes and litigation about whether particular payments are interest for section 163(j) purposes.

A further concern, over providing a narrower definition of interest, is that it could encourage taxpayers to engage in transactions that provide financing while generating deductions economically similar to interest but that were not defined as interest for the purposes of section 163(j). There are several reasons why curbing such taxpayer behavior would be beneficial. First, the ability of taxpayers to engage in such transactions is correlated with the size of the trade or business, with large businesses more likely to benefit from such avoidance strategies than small businesses. Second, when the deciding factor for using such transactions is the tax benefit of avoiding a section 163(j) limitation, then such transactions would impose more cost or risk on the taxpayer than using a traditional debt instrument. Engaging in such transactions is an inefficient use of resources. Third, such avoidance strategies may discourage taxpayers from shifting to a less leveraged capital structure, and thus would counteract the intention of the statute to reduce the prevalence of highly-leveraged firms and the probability of systemic financial distress. Fourth, greater use of financing outside of conventional debt instruments may make it more difficult for financial institutions to determine the overall level of leverage and credit risk of firms seeking financing, which may distort the allocation of capital across businesses away from firms and investments with less credit risk.

The final regulations prescribe a definition of interest that is similar to the definition of interest in the proposed regulations although with changes made in response to comments.[4] There are three general types of changes: (1) Changes are made to the proposed regulations that modify, and generally limit, to what extent certain amounts are included under the definition of interest for the purposes of section 163(j). (2) Several items deemed to be interest for the purpose of section 163(j) under proposed § 1.163(j)–1(b)(20)(iii) are not included in the final regulations. (3) The anti-avoidance rule in proposed § 1.163–1(b)(20)(iv) is modified to include a principal purpose test and now also applies to situations where a taxpayer seeks to artificially increase the amount of interest income.

To the extent that these changes narrow the definition of interest that is subject to the section 163(j) limitation relative to the proposed regulations, they are expected to (i) reduce the cost of financing for taxpayers, an effect that is expected to increase investment by these taxpayers, and (ii) increase the proportion of that financing that might generally be considered debt-financed. The first effect occurs because taxpayers can deduct without limitation costs from a larger set of financial instruments under the final regulations, relative to the proposed regulations. They will choose these instruments only if the cost of obtaining funds through those instruments is lower than what would have been available under the proposed regulations. By extension, this change lowers the overall cost of financing for taxpayers. A lower cost of financing is associated with greater investment by taxpayers, all other things equal. The second effect occurs because the larger set of financial instruments for which taxpayers can deduct expense without limitation (under the final regulations,

[4] The proposed regulations represent the regulatory alternative to which the final regulations are compared in the following analysis.

relative to the proposed regulations) generally consists of instruments that have a greater share of debt characteristics, rather than equity characteristics. To the extent that taxpayers use these instruments to a greater degree under the final regulations relative to the proposed regulations, the share of debt-financing will increase. Congress has generally expressed the view that excessive debt-financing may be a less efficient capital structure for firms. See Senate Budget Explanation of the Bill at 165.

Because the final regulations define interest based on the intent and purpose of the statute and generally treat similar taxpayers similarly and similar economic activity similarly, the Treasury Department and the IRS have determined that the net result under these final regulations is a more efficient allocation of capital across taxpayers relative to regulatory alternatives, within the context of the intent and purpose of the statute.

The Treasury Department and the IRS have not undertaken quantitative estimates of the change in the level or nature of economic activity arising from the final regulations relative to the proposed regulations due to limitations on available data, but to the extent possible has provided further below an estimate of the quantity of potentially affected taxpayers and volume of transactions. Consider, for example, the treatment of guaranteed payments for the use of capital provided by a partner to a partnership, a financial arrangement that has both equity and debt characteristics. The proposed regulations included guaranteed payments to capital in the definition of interest while the final regulations do not, except to the extent that they are covered by other provisions of the final regulations. The Treasury Department and the IRS have not undertaken quantitative estimates of this regulatory decision because we do not have readily available data or models to measure with sufficient precision: (i) The volume and nature of guaranteed payments to capital and other financial instruments that taxpayers might use if the final regulations were in effect; (ii) the volume and nature of guaranteed payments and other financial instruments that taxpayers might have used if the proposed regulations were in effect; and (iii) the types of economic activities that partnerships might undertake under these two financial portfolios. Regarding item (iii), the Treasury Department and the IRS do not have readily available data or models to predict how economic activity might differ under debt-financed versus equity-financed investment for the sets of instruments affected by these final regulations.

Compliance costs are also expected to be lower for those transactions that are not subject to the section 163(j) limitation under the final regulations and that would be subject to the limitation under the proposed regulations. Generally, this is because taxpayers would be less likely to need to calculate the section 163(j) limitation and less likely to need to track unused interest deductions that are carried forward to future tax years. For most taxpayers, this impact on compliance costs is expected to be relatively small. However, for certain taxpayers using hedging transactions, calculating the amount of interest associated with the transactions would be burdensome and not including such transactions in the definition of interest lowers compliance costs to a greater degree. The Treasury Department and the IRS have not estimated the reduction in compliance costs for these taxpayers (under the final regulations, relative to the proposed regulations) because we do not have data or models that are suitable for this estimation.

The specific changes made with regard to items (1), (2), and (3) are discussed in further detail here.

(1) The final regulations change (relative to the proposed regulations) how amounts from certain transactions will be considered interest for the purposes of section 163(j). There are two main forms of transactions that are affected:

Treatment of swaps. The proposed regulations treated a non-cleared swap with significant non-periodic payments as two separate transactions consisting of an on-market, level payment swap and a loan (the embedded loan rule).[5] The time value component associated with the embedded loan is recognized as interest expense to the payor and interest income to the recipient. The treatment of cleared swaps was not specified in the proposed regulations. The final regulations add two exceptions to the embedded loan rule. Specifically, the final regulations add exceptions for cleared swaps and for those non-cleared swaps that require the parties to meet the margin or collateral requirements of a federal regulator (or requirements that are substantially similar to a federal regulator). Relative to the proposed regulations this treatment will discourage taxpayers from using swaps that are unregulated and dissimilar to regulated swaps, because under the final regulations only such swaps will require the time value component associated with the embedded loan to be treated as interest. One reason for excepting both regulated and non-regulated collateralized swaps from the definition of interest is that the repayment risk of using such transactions is small, while the non-collateralized swaps are more risky as individual transactions and would be likely to contribute to the overall riskiness of the financial system.

Substitute interest payments. The proposed regulations provided that certain substitute interest payments will be treated as interest for the purposes of section 163(j).[6] The final regulations modify the treatment of substitute interest payments by only including such transactions as interest when the transaction is not part of the ordinary course of business of the taxpayer. The Treasury Department and the IRS have determined that the ordinary course rule in the final regulations provides an appropriate and effective limit on the treatment of substitute interest as interest for section 163(j) purposes. This change has the effect of reducing the amount of substitute interest payments that will be deemed interest for the purpose of section 163(j) relative to the proposed regulations.

For taxpayers that use substitute interest payments in the ordinary course of business, the final regulations may lower the after-tax cost of such transactions and such taxpayers are more likely to use transactions with substitute interest payments relative to the proposed regulations. The Treasury Department and the IRS do not have readily available data or models to estimate either (i) the change in financing arrangements, including both substitute interest payments and other financial instruments, that will be used by taxpayers under this provision of the final regulations relative to the proposed regulations, or (ii) the change in the volume or nature of economic activity by these taxpayers given these financing arrangements.

(2) The items removed by the final regulations from the definition of interest in the proposed regulations include debt issuance costs, guaranteed payments for the use of capital provided

[5] A cleared swap is a collateralized swap that was cleared by a derivatives clearing organization or by a clearing agency. A non-cleared swap is a swap that has not been so cleared.

[6] A substitute interest payment is a payment, made to the transferor of a security in a securities lending transaction or a sale-repurchase transaction, of an amount equivalent to an interest payment which the owner of the transferred security is entitled to receive during the term of the transaction. This provision applies to substitute interest payments as described in § 1.861–2(a)(7).

by a partner to a partnership, and hedging transactions.[7] Under the final regulations, these items can still be considered interest under the anti-avoidance rule. These items share some characteristics with interest, but comments received on the proposed regulations indicate there is not a consensus that such items should always be defined as interest. Removing these items from the definition of interest lowers compliance costs for taxpayers in some cases relative to the proposed regulations. However, not including these items in the definition of interest increases uncertainty regarding whether amounts from certain transactions will be treated as interest under the anti-avoidance rule, and more disputes are likely to arise between taxpayers and the IRS.

The final regulations do not include debt issuance costs, such as legal fees for document preparation, in the definition of interest. Debt issuance costs are usually small relative to total interest payments in a lending transaction and often the payments are made to a third-party who is not the lender. Hence, there is limited ability for taxpayers to be able to disguise interest payments as debt issuance costs. The primary effect of not including debt issuance costs in the definition of interest is to decrease the after-tax cost of debt financing.

The final regulations do not include hedging transactions in the definition of interest. Taxpayers could have multiple reasons for engaging in hedging transactions other than just to lower the amount of interest expense, such as a reduction in risk. Not including hedging transactions in the definition of interest should decrease administration and compliance costs compared to the treatment in the proposed regulations since it can be difficult to separate the time value component from the insurance aspects of a hedging transaction. Under the final regulations, taxpayers are more likely to use hedging relative to the proposed regulations due to the decline in compliance costs and due to the reduced after-tax cost of using hedges.

The final regulations do not include guaranteed payments in the definition of interest. Guaranteed payments for the use of capital provided by a partner to a partnership have both equity and debt characteristics. The partner who provided the capital is an owner of the business, but also receives payments that are similar to interest. Removing guaranteed payments from the definition of interest lowers the after-tax cost of such financing for some taxpayers and may lead these taxpayers to increase the fraction of financing through capital with guaranteed payments relative to other financial instruments. The Treasury Department and the IRS do not have readily available data or models to project the change in the volume or nature of businesses' economic activities that would arise as a consequence of this change in the tax treatment of guaranteed payments to capital, relative to the proposed regulations.

(3) The final regulations also modify the anti-avoidance rule found in proposed § 1.163–1(b)(20)(iv) relative to the proposed rule. One change is that the anti-avoidance rule not only applies to financing transactions used to avoid the classification of financing expense as interest expense, but also excludes transactions that artificially increase the taxpayer's interest income from being included as interest income. The final regulations also add a principal purpose condition to the anti-avoidance rule. That is, the anti-avoidance rule in the final regulations only applies to amounts where a principal purpose of the taxpayer for engaging in a transaction is to artificially reduce the amount of net business interest expense, whether this stems from a decrease in the amounts reported as interest expense or an increase in the amounts reported as interest income. This symmetric anti-avoidance rule adopted under the final regulations, applying to both interest income and interest expense, increases the number of transactions to which the rule could potentially apply compared to the proposed regulations. However, including a principal purpose test in the anti-avoidance rule will decrease how often the rule would potentially apply to transactions relative to the proposed rule.

The anti-avoidance rule is an important component of the definition of interest because it is difficult for the Treasury Department and the IRS to specifically categorize every type of transaction already in practice or to anticipate future innovations in financial transactions. Relative to regulatory alternatives, the anti-avoidance rule will help limit the ability of taxpayers to structure transactions in such a way that would allow deductible expenses that are economically similar to interest and frustrate the application of the statute. In summary, the definition of interest in the final regulations provides clarity to taxpayers and the IRS regarding which specific transactions and types of transactions generate interest subject to the section 163(j) limitation, which should lower compliance and administrative costs relative to providing no definition or a narrower definition of interest. The Treasury Department and the IRS further have determined that the definition of interest specified under the final regulations will encourage a more efficient allocation of capital and use of financing across taxpayers relative to the no-action baseline, within the context of the intent and purpose of the statute.

Number of Affected Taxpayers. The Treasury Department and the IRS estimate that the number of partnerships potentially affected by the change in treatment to guaranteed payments for the use of capital provided by a partner to a partnership is 6,000. This is the number of partnerships in tax year 2017 with more than $25 million in gross receipts that also report paying deductible guaranteed payments. The amount of total guaranteed payments reported by these partnerships is approximately $30 billion. However, it is not known to what extent these guaranteed payments are made to capital or labor, as the tax form for that tax year did not distinguish between the two types of guaranteed payments. Beginning in 2019, Form 1065 will separately report those two types of guaranteed payments.

It is not possible to provide a meaningful estimate of the number of taxpayers potentially affected by the final regulations that have deductible debt issuance costs, substitute interest payments, or amounts from swaps or hedging transactions, because those amounts are not reported separately on a tax return.

4. Economic Effects of Provisions Not Substantially Revised From the Proposed Regulations

a. Calculation of Excess Business Interest Expense, Excess Business Interest Income, and Excess Taxable Income for Partnerships and S Corporations

The statute applies broadly to different types of entities, including passthrough entities, such as partnerships and S corporations. The statute specifies that the section 163(j) limitation applies at the entity level for a partnership but that items such as excess business interest expense and excess taxable income must be allocated to partners for a variety of reasons including to compute their own 163(j) limitation. The statute further specifies

[7] Commitment fees are also not included in the definition of interest in the final regulations, but may be addressed as part of another guidance project on the treatment of fees relating to debt instruments and other securities in the future.

that the items should be allocated in the same manner as ''nonseparately stated taxable income or loss of the partnership''; however, this concept had not previously been defined by statute or regulations prior to the proposed regulations. In the absence of guidance, partnerships would have significant uncertainty in determining which partners receive excess items. This uncertainty could lead one partnership to undertake an activity that another partnership might decline to take based solely on different expectations about tax treatment of interest income rather than underlying productivity differences or economic signals.

The final regulations provide guidance on how to allocate partnership excess business interest expense, excess business interest income, and excess taxable income to partners. The allocation method detailed in the final regulations follows a number of principles. First, it ensures that the sum of the excess items at the partner level is equal to the total at the partnership level. Second, it ensures that the partnership does not allocate excess business interest expense to a partner that was allocated items that include ATI and business interest income that supported the partnership's deductible business interest expense (unless the partner was allocated more interest expense than its share of deductible business interest expense). Finally, it ensures that the partnership allocates any excess taxable income or excess business interest income to partners that are allocated more items comprising ATI or business interest income than necessary to support their allocation of business interest expense.

The final regulations thus provide a method to ensure that all partnerships allocate these items consistently and in a way that matches income and interest expense, thus promoting economically efficient investment decisions across taxpayers and across financing options, relative to the no-action baseline.

b. Interest Income Inclusion for Owners of Partnerships and S Corporations

The final regulations ensure that, for owners of partnerships and S corporations, business interest income is used only once, at the entity level, in offsetting business interest expenses. It thereby avoids exacerbating the incentive to seek out interest income relative to other forms of less economically productive income in order to avoid the section 163(j) limitation, relative to the no-action baseline.

c. Rules Related to Excepted Businesses

For purposes of section 163(j), the statute states in section 163(j)(7) that the term ''trade or business'' does not include certain regulated utilities, or an electing real property trade or business or an electing farming business. The final regulations clarify whether a trade or business could elect as a farming business or a real property trade or business and thus be excepted from section 163(j). Specifically, § 1.163(j)–9 provides guidance in applying the rules for farming and real property trade or business elections. For an electing real property trade or business and electing farming business, the statue specifies that ''any such election shall be made at such time and in such manner as the Secretary shall prescribe, and once made, shall be irrevocable.'' Therefore § 1.163(j)–9 provides taxpayers with the time and manner for electing real property trades or businesses and electing farming businesses. In addition, the final regulations define the conditions under which an election terminates.

In the absence of specific guidance, taxpayers may engage in behavior that counteracts the intent and purpose of the statute and would not otherwise be taken except to avoid the irrevocable nature of the election the statute specified. The final regulations increase the likelihood that taxpayers interpret the 'irrevocable' designation similarly and do not engage in tax-motivated behavior by appearing to cease operations in an effort to change an irrevocable designation.

In addition, § 1.163(j)–9(h) provides a safe harbor for certain REITs to elect to be electing real property trades or businesses. A special rule applies to REITs for which 10 percent or less of the value of the REIT's assets are real property financing assets. Under this rule, all of the assets of the REIT are treated as real property trade or business assets. The benefit of the safe harbor is to provide REITs the same tax treatment and apply the same general rules as apply to other taxpayers, an economically efficient approach. The special rule threshold of 10 percent for real property financing assets has the benefit of maintaining consistency with section 856(c)(4), which uses the same values for the REIT asset test at the close of the REIT's taxable year. Taxpayers will benefit in reduced compliance time and cost in applying new rules if the rules are consistent with other rules that they must comply with under the Code. An estimate of the compliance cost savings that would be due to this cross-code consistency, relative to regulatory alternatives, is beyond the capabilities of the IRS's compliance model.

In addition, the final regulations provide a rule that stipulates that if at least 80 percent of a trade or business's real property (by fair market value) is leased to a trade or business under common control with the real property trade or business, the trade or business cannot make an election to be an electing real trade or business. In the absence of such a rule, taxpayers could restructure their business such that real estate components of non-real estate businesses are separated from the rest of their business to artificially reduce the application of section 163(j) by leasing the real property to the taxpayer and electing this ''business'' to be an excepted real property trade or business. Therefore, the prime benefit of this rule is to preserve the intent of the statute of allowing elections in the real property sector without incentivizing other sectors of the economy to restructure their business for the sole intent of avoiding the section 163(j) limitation.

The Treasury Department and the IRS received no comments requesting that the percentage amounts be changed.

Number of Affected Taxpayers. The Treasury Department and the IRS project that nearly 3,500 REITs are potentially affected by the provision in the final regulations that allows REITs for which 10 percent or less of the value of the REIT's assets are real property financing assets to elect to treat all of its assets as allocable to an excepted real property trade or business. This estimate is based the number of REITs in the SOI sample of corporate taxpayers for 2017 that identify as an Equity REIT. An Equity REIT is identified by a check-box on form 1120–REIT where the choice is Equity REIT or Mortgage REIT. The Mortgage REIT category should be chosen by the taxpayer if the primary source of gross receipts is derived from mortgage interest and fees. These Equity REITs reported $1.7 trillion in total assets.

The Treasury Department and the IRS project that roughly 2.8 million filers are potentially affected by provisions of the final regulations that affect electing real property trades or businesses or electing farm businesses. This estimate is based on a count of all filers with NAICS codes starting with 111 or 112 (farming), and 531 (real property) with at least $10 million in gross receipts in taxable year 2017.

d. Allocation Rules Between Excepted and Non-Excepted Trades or Businesses

The statute is silent over how ATI, interest income, and expense should be allocated between excepted and non-excepted trades or businesses. Thus, the Treasury Department and the IRS decided to provide taxpayers with an allocation method. Because allocation, by whatever method, is costly for taxpayers, the final regulations further provide that allocation is only required when the share of the asset tax basis in both the excepted and the non-excepted trades or businesses exceeds 10 percent. In other words, if the share for either excepted or non-excepted trades or businesses is 10 percent or less, allocation is not required. The Treasury Department and the IRS received no comments that addressed the 10 percent threshold provided in this provision.

In terms of the allocation method, the Treasury Department and the IRS decided in the final regulations to require taxpayers to allocate interest expense and interest income between related excepted and non-excepted trades or businesses based on the relative amounts of the taxpayer's adjusted tax basis in the assets used in its excepted and non-excepted trades or businesses. As discussed in the Explanation of Provisions section of the proposed regulations, this general method of allocation reflects the fact that money is fungible and the view that interest expense is attributable to all activities and property, regardless of any specific purpose for incurring an obligation on which interest is paid. This asset basis approach is consistent with the regulations under section 861. Because this approach is familiar to taxpayers and consistent with other parts of the Code, taxpayers benefit in reduced time and cost spent learning and applying the rules, relative to alternative regulatory approaches. An estimate of the compliance cost savings that would be due to this familiarity and cross-code consistency, relative to regulatory alternatives, is beyond the capabilities of the IRS's compliance model.

The Treasury Department and the IRS considered several alternatives to this asset basis approach for allocating interest income and expense. First, a tracing approach was considered whereby taxpayers would be required to trace disbursements of debt proceeds to specific expenditures. However, tracing would impose a significant compliance burden on taxpayers due to the complexity of matching interest income and expense among related companies. Further, it is not clear how taxpayers would retroactively apply a tracing regime to existing debt. In particular, because C corporations would have had no reason to trace the proceeds of any existing indebtedness, imposing a tracing regime on existing indebtedness would require corporations to reconstruct the use of funds within their treasury operations at the time such indebtedness was issued, even if the issuance occurred many years ago, and even if the funds were used for a myriad of purposes across a large number of entities. Such an approach would impose substantial compliance costs and may be impractical or even impossible for indebtedness issued years ago.

Moreover, because money is fungible, a tracing regime would be distortive and subject to manipulation. Although taxpayers are impacted from both a commercial and tax perspective by the amount of capital raised through the issuance of equity and indebtedness, any trade or business conducted by a taxpayer is generally indifferent to the source of funds. As a result, if taxpayers were allowed to use a tracing regime to allocate indebtedness to excepted trades or businesses, there would be an incentive to treat excepted trades or businesses as funded largely from indebtedness, and to treat non-excepted trades or businesses as funded largely from other types of funding, such as equity funding, despite the fact that, as an economic matter, all of a taxpayer's trades or businesses are funded based on the taxpayer's overall capital structure.

The Treasury Department and the IRS rejected a tracing approach because the complexity of such an approach could be more difficult for taxpayers and the IRS to administer and would create too great an incentive to structure financing with the sole purpose of avoiding the application of the statute, relative to the final regulations. The assumption that a trade or business is indifferent to its source of funds may not be appropriate in cases in which certain indebtedness is secured by the assets of the trade or business and cash flow from those assets is expected to support the payments required on the indebtedness. The final regulations provide for a limited tracing rule in those cases.

The Treasury Department and the IRS also considered allocating interest expense based on the relative fair market value of the assets used in excepted and non-excepted trades or businesses. However, determinations of fair market value frequently are burdensome for taxpayers, which may have numerous assets without a readily established market price. For this reason, disputes between taxpayers and the IRS over the fair market value of an asset are a common and costly occurrence. In the TCJA, Congress repealed the use of fair market value in the apportionment of interest expense under section 864 of the Code (see section 14502(a) of the TCJA) and claimed that the ability to elect to allocate interest expense under section 864 on the basis of fair market value of assets has led to inappropriate results and needless complexity. See Senate Budget Explanation of the Bill at 400. Thus, the Treasury Department and the IRS have determined that allocating interest expense based on relative amounts of asset basis is more appropriate than a regime based on the relative fair market value of assets.

The Treasury Department and the IRS also considered allocating interest expense to excepted and non-excepted trades or businesses based on the relative amounts of gross income generated by such trades or businesses. However, gross income is more variable and volatile than asset basis, in part because it is based on an annual measurement. Methods could be developed to look at multiple years of gross income through an averaging or other smoothing methodology, but any such approach would necessarily create a number of difficult technical questions because the income of different trades or businesses may be subject to differing business cycles and the taxpayers may exert control over the timing of income items, which may lead taxpayers to make tax-driven business decisions with no accompanying general economic benefit. In the TCJA, Congress also repealed the use of gross income in the apportionment of interest expense under section 864 of the Code (see section 14502(a) of the TCJA). Thus, the Treasury Department and the IRS have determined that allocating interest expense based on relative amounts of asset basis is more appropriate than a regime based on the relative amounts of gross income.

Number of Affected Taxpayers. The Treasury Department and the IRS estimate that roughly 83,000 firms had allocated interest income and expenses among multiple trades or businesses in tax year 2015 and thus are potentially affected by provisions of the final regulations that affect the annual allocation statement. This estimate is based on a count of all Forms 1120, 1120S, and 1065 in tax year 2015 in real estate, farming, and public utilities industries that had over $25 million in gross receipts.

II. Paperwork Reduction Act

The collections of information contained in the final regulations have been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C.

3507(d)). 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 control number assigned by the Office of Management and Budget.

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

A. Collections of Information Imposed by the Regulations

The collections of information imposed directly by these regulations are contained in §§ 1.163(j)–1(b)(15)(iii), 1.163(j)–2(b)(2)(ii), 1.163(j)–2(b)(3), 1.163(j)–9 and 1.163(j)–10.

The collection of information in §§ 1.163(j)–1(b)(15)(iii) and 1.163(j)–9, the election statement, is required for taxpayers to make a one-time election to treat their regulated utility trade or business, real property trade or business or farming trade or business as an electing excepted regulated utility trade or business, electing real property trade or business under section 163(j)(7)(B) or an electing farming business under section 163(j)(7)(C). The election to be an excepted regulated utility trade or business was not in the proposed regulations. The scope of taxpayers eligible to make an election to be an excepted real property or farming trade or business has changed from the proposed regulations. As discussed in part X of the Summary of Comments and Explanation of Revisions section, under the proposed regulations, taxpayers that met the small business exemption test under section 448(c) were not able to make an election for their trade or business to be an electing real property trade or business or an electing farming business because they were already not subject to the limitation. Under the final regulations, those taxpayers are eligible to make a protective election. Additionally, under the proposed regulations, it was unclear whether taxpayers that were unsure of whether their activity constitutes a trade or business under section 162 could make an election. The final regulations clarify that a taxpayer that is unsure whether its activity constitutes a trade or business under section 162 is eligible to make an election.

The collections of information in §§ 1.163(j)–2(b)(2)(ii) and 1.163(j)–2(b)(3) are required to make two elections relating to changes made to section 163(j)(10) by the CARES Act. The election under § 1.163(j)–2(b)(2)(ii) is for a taxpayer to use the 30 percent ATI limitation instead of the 50 percent ATI limitation when calculating the taxpayer's section 163(j) limitation for a 2019 or 2020 taxable year, as provided in section 163(j)(10)(A)(i) and (iii). The election under § 1.163(j)–2(b)(2) is for a taxpayer to use the taxpayer's ATI for the last taxable beginning in 2019 as its ATI for any taxable year beginning in 2020, as provided in section 163(j)(10)(B). Revenue Procedure 2020–22 describes the time and manner for making these elections. See also § 1.163(j)–2(b)(4).

Taxpayers make the elections by timely filing a Federal income tax return or Form 1065, including extensions, an amended Federal income tax return, amended Form 1065, or administrative adjustment request, as applicable. More specifically, taxpayers complete the Form 8990, Limitation on Business Interest Expense under Section 163(j), using the 30 percent ATI limitation and/or using the taxpayer's 2019 ATI, as applicable. No formal statements are required to make these elections. Accordingly, for Paperwork Reduction Act purposes, the reporting burden associated with the collections of information in §§ 1.163(j)–2(b)(2)(ii) and 1.163(j)–2(b)(3) will be reflected in the IRS Form 8990 Paperwork Reduction Act Submissions (OMB control number 1545–0123).

The collection of information in § 1.163(j)–10, the allocation statement, is required for taxpayers to demonstrate how they allocated their interest expense, interest income, and other items of income and deduction between excepted and non-excepted trades or businesses. The mechanics of the allocation statement, and the scope of taxpayers required to file the allocation statement, have not changed from the proposed regulations.

Section 1.163(j)–10 in the final regulations contains another collection of information, an allocation methodology change request, requiring taxpayers to request the Commissioner's permission to change a methodology for allocating the basis in an asset that is used in multiple trades or businesses if the request is being made within five years of any prior change. This requirement does not create a new burden because the allocation methodology change request is made by following the procedures for requesting a letter ruling in section 7.01 of Revenue Procedure 2020–1, 2020–1 IRB 1. Revenue Procedure 2020–1 was approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1545–0123.

In 2018, the Treasury Department and the IRS considered developing a form election and allocation statement under §§ 1.163(j)–9 and 1.163(j)–10 for taxpayers to make the one-time election and to demonstrate their interest allocation. To minimize taxpayer burden, the Treasury Department and the IRS decided that, for now, taxpayers should be allowed to use their own election form and allocation statement. In the future, if the Treasury Department and the IRS develop election or allocation form, the draft versions of the forms will be posted for comment at *https://apps.irs.gov/app/picklist/list/draftTaxForms.html.*

Certain forms have been modified with simple questions to signal whether the taxpayer is subject to section 163(j). The Treasury Department and the IRS are considering modifying certain forms with a checkbox to note that a taxpayer has made an election for a trade or business to be an electing real property trade or business or electing farming business.

For the allocation methodology change request in § 1.163(j)–10, the Treasury Department and the IRS initially determined that taxpayers should file a change request any time there is a change in methodology. However, a change in allocation methodology presents a burden for taxpayers. The disadvantages of changing an allocation methodology regularly, including the administrative and accounting costs associated with any such change, outweigh the advantages of changing an allocation methodology regularly. Accordingly, the Treasury Department and the IRS do not anticipate taxpayers using the allocation methodology change request regularly. The final regulations require the request to be made only if a change has not been made in the past 5 years. To minimize any compliance burden, the procedures in Revenue Procedure 2020–1, which are familiar to taxpayers, apply for the allocation methodology change request.

B. Burden Estimates

The following burden estimates are based on the information that is available to the IRS, and have been updated from the proposed regulations to take into account the new election for certain regulated utility trades or businesses, the increased scope of potential filers for the election statement and to use 2017 Statistics of Income (SOI) tax data where available.

The most recently available 2017 SOI tax data indicates that approximately 8,208 filers are possible for the one-time election to opt out of the section 163(j) limitation as an electing excepted regulated utility trade or business. This estimate was based on a count of Form 1065, 1065B, 1120 and 1120–S filers with NAICS codes starting with 2211 (electric power generation, transmission and distribution), 2212 (natural gas distribution), and 2213 (water, sewage and other systems).

The 2017 SOI tax data indicates that approximately 2,838,981 filers are possible for the one-time election to opt out of the section 163(j) limitation as an electing real property trade or business or as an electing farming business were the statute then in effect. This estimate is based on a count of all filers with NAICS codes starting with 111 or 112 (farming), and 531 (real property) with at least $10 million in gross receipts in taxable year 2017. The increase in potential filers from the number provided in the proposed regulations is due exclusively to the fact that the final regulations provide that taxpayers that satisfy the small business exemption are eligible to file an election.

For the election to use the 30 percent ATI limitation for a 2019 or 2020 taxable year under § 1.163(j)–2(b)(ii), while any taxpayer subject to the section 163(j) limitation is eligible to make the election, the Treasury Department and the IRS estimate that only taxpayers that actively want to reduce their deductions will make this election. The application of the base erosion minimum tax under section 59A depends, in part, on the amount of a taxpayer's deductions. Accordingly, the Treasury Department and the IRS estimate that taxpayers that are subject to both the base erosion minimum tax under section 59A and section 163(j) are the potential filers of this election. Using the 2017 SOI tax data, the Treasury Department estimate that 3,376 firms will make the election. This estimate was determined by examining the number of C corporations with at least $500,000,000 in gross receipts, that do not have an NAICS code associated with a trade or business that is generally not subject to the section 163(j) limitation (2211 (electric power generation, transmission and distribution), 2212 (natural gas distribution), 2213 (water, sewage and other systems), 111 or 112 (farming), 531 (real property)).

For the election to use the taxpayer's 2019 ATI in 2020 under § 1.163(j)–2(b)(3), the Treasury Department and the IRS estimate that 72,608 firms will make the election. This figure was determined, using 2017 SOI tax data, by examining Form 1040, Form 1120, Form 1120S, and Form 1065 filers with more than $26M in gross receipts, that have reported interest expense, and do not have an NAICS code associated with any trade or business that is generally not subject to the section 163(j) limitation.

The Treasury Department and the IRS continue to estimate the same number of filers, 82,755, for the annual allocation statement as was projected in the proposed regulations. Using the 2015 SOI tax data, the Treasury Department and the IRS estimate that 82,755 firms will have allocated interest income and expenses among multiple trades or businesses, some of which are excepted from the section 163(j) limitation and some that are not. This estimate is a count of all tax Forms 1120, 1120S, and 1065 in real estate, farming, and public utilities industries that had over $25 million in gross receipts. While the number of affected taxpayers will increase with growth in the economy, the Treasury Department and the IRS expect that the portion of affected taxpayers will remain approximately the same over the foreseeable future.

The time and dollar compliance burden are derived from the Business Taxpayers Burden model provided by the IRS's Office of Research, Applied Analytics, and Statistics (RAAS). This model relates the time and out-of-pocket costs of business tax preparation, derived from survey data, to assets and receipts of affected taxpayers along with other relevant variables. See ''Tax Compliance Burden'' (John Guyton et al, July 2018) at *https://www.irs.gov/pub/irs-soi/d13315.pdf.* A respondent may require more or less time than the estimated burden, depending on the circumstances.

The burden estimates listed in the below table attempt to capture only those discretionary changes made in these proposed regulations, and may not include burden estimates for forms associated with the statute. Changes made by the Act or through new information collections are captured separately in forthcoming published ''Supporting Statements'' for each of these forms and will be aggregated with the estimates provided below to summarize the total burden estimates for each information collection listed below. Those total burden estimates will be available for review and public comment at *https://www.reginfo.gov/public/Forward?SearchTarget=PRA&textfield.* The Treasury Department and the IRS request comment on these estimates.

	Likely respondents	Estimated number of respondents	Estimated average annual burden hours per respondent	Estimated total annual reporting burden (hours)	Estimated monetized burden @ $95/hour ($millions)	Estimated frequency of responses
Section 1.163(j)–1(b)(15)(iii) (one-time election statement (2017 Levels).	Corporations and partnerships with regulated utility trades or businesses.	8,028 business respondents (including Forms 1120, 1120–S, and 1065 filers).	0 to 30 minutes (estimated average: 15 minutes).	2,007	$190,665 ...	One-time.
Section 1.163(j)–2(b)(ii) (election to apply the 30 percent ATI percentage).	C corporations with more than $500 M in gross receipts.	3,376 business respondents (Form 1120 filers).	See Form 8990 ..	See Form 8990.	See Form 8990.	See Form 8990.
Section 1.163(j)–2(b)(3) (election to use 2019 ATI as 2020 ATI).	Individuals, corporations, and partnerships with more than $26 M in gross receipts and not part of an excepted trade or business.	72,608 business respondents (including Form 1120, Form 1120–S, and Form 1065 filers).	See Form 8990 ..	See Form 8990.	See Form 8990.	See Form 8990.

	Likely respondents	Estimated number of respondents	Estimated average annual burden hours per respondent	Estimated total annual reporting burden (hours)	Estimated monetized burden @ $95/hour ($millions)	Estimated frequency of re-sponses
Section 1.163(j)–9 (one-time election statement) (2017 Levels).	Individuals, corporations, and partnerships with real property or farming trades or businesses with gross receipts exceeding $10 million.	2,838,981 business respondents (all filers).	0 to 30 minutes (estimated average:15 minutes).	70,746	67.4	One-time.
Section 1.163(j)–10 (annual allocation statement) (2015 Levels).	Individuals, corporations, and partnerships (1) with more than one trade or business (at least one of which is a real property or farming trade or business), and (2) public utilities, with gross receipts exceeding the statutory threshold of $25 million.	82,755 business respondents (including Forms 1120, 1120–S, and 1065 filers).	15 minutes to 2 hours (estimated average: 1 hour).	82,755	7.9	Annually.
Section 1.163(j)–10 (change in allocation methodology request).	Individuals, corporations, and partnerships that want to change their methodology for allocating basis among two or more trades or businesses, and (1) with more than one trade or business (at least one of which is a real property or farming trade or business), and (2) public utilities, with gross receipts exceeding the statutory threshold of $25 million.	See Rev. Proc. 2020–1.	See Rev. Proc. 2020–1.	See Rev. Proc. 2020–1.	See Rev. Proc. 2020–1.	On occasion.
Section 1.163(j)–10 (one-time start-up cost to develop procedures for filing an annual allocation statement) (2017 Levels).	Same as above	82,755	4 hours (start-up burden).	331,020	31.4	One-time.
Three year monetized burden estimate.					40.8	Three year annual average.

The three-year annual average of the monetized burden for the information collection and resulting from discretionary requirements contained in this rulemaking is estimated to be 40.9 million ($2017) ([($190, 665) + ($67.4 million + $31.4 million) + ($7.9 million × 3)]/3). To ensure more accuracy and consistency across its information collections, the IRS is currently in the process of revising the methodology it uses to estimate burden and costs. Once this methodology is complete, the IRS will provide this information to reflect a more precise estimate of burdens and costs.

C. Forms

The IRS has developed Form 8990, ''Limitation on Business Interest Expense Under Section 163(j),'' to facilitate reporting of the limitation. The form is posted at *https://www.irs.gov/pub/irs-access/f8990_accessible.pdf.* The Form 8990 instructions are posted at *https://www.irs.gov/pub/irs-pdf/i8990.pdf.* The Form 1120 series and the Form 1065 have been revised to include a question to alert taxpayers of the need to file a Form 8990. The instructions to those and other forms have been revised to include information about the Form 8990.

As described previously, the reporting burdens associated with the information collections in the proposed regulations are included in the aggregated burden estimates for OMB control number 1545–0123 (in the case of filers of Form 1120, Form 1065 and Form 8990), 1545–0074 (in the case of individual filers), and 1545–0123 (in the case of filers under Revenue Procedure 2020–1).

The Treasury Department and the IRS request comment on all aspects of information collection burdens related to these regulations, including estimates for how much time it would take to comply with the paperwork burdens described previously for each relevant form and ways for the IRS to minimize the paperwork burden. In addition, when available, drafts of IRS forms are posted for comment at *https://apps.irs.gov/app/picklist/list/draftTaxForms.htm.*

Form/revenue procedure	Type of filer	OMB No(s).	Status
	Business (NEW Model)	1545–0123	Published in the **Federal Register** on 10/8/18. Public comment period closed on 12/10/18.
	Link: *https://www.federalregister.gov/documents/2018/10/09/2018-21846/proposed-collection-comment-request-for-forms-1065-1065-b-1066-1120-1120-c-1120-f-1120-h-1120-nd.*		

Form/revenue procedure	Type of filer	OMB No(s).	Status
	Individual (NEW Model)	1545–0074	Limited scope submission (1040 only) on 10/11/18 at OIRA for review. Full ICR submission for all forms in 2019.
	Link: *https://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=201808-1545-031.*		
Revenue Procedure 20201	IRS Research estimates ...	1545–0123	Published in the Internal Revenue Bulletin on January 2, 2020.
	Link: *https://www.irs.gov/irb/2020-01_IRB.*		

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 within the meaning of section 601(6) of the Regulatory Flexibility Act (small entities). This certification can be made because the Treasury Department and the IRS have determined that the regulations may affect a substantial number of small entities but have also concluded that the economic effect on small entities as a result of these regulations is not expected to be significant.

When enacted, the section 163(j) limitation generally applied to taxpayers with average annual gross receipts exceeding $25 million. The gross receipts threshold for general applicability of the section 163(j) limitation increased to $26 million in 2020. The threshold will be adjusted annually for inflation. However, under the final regulations, small taxpayers operating regulated utility trades or businesses, real property trades or businesses and farming trades or businesses are now eligible to protectively elect out of the election. Accordingly, the regulations in §§ 1.163(j)–1 and –9 may apply to small business filers that operate regulated utility trades or businesses, real property trades or businesses or farming trades or businesses. Those taxpayers may choose to make a protective election, such that they are not subject to the limitation if their average annual gross receipts for the three prior tax years eventually exceeds $26 million (for 2020). Although the exact number of small entities that will make an election is unknown, an upper bound on the number of potentially affected entities is 10.5 million. This number was determined by looking at, for the 2017 taxable year, the number of Form 1120, 1120–S, 1120–REIT, 1065, and individual business filers with more than $10M in gross receipts that have NAICS codes commonly associated with real property trades or businesses or farming businesses.

If a taxpayer chooses to make the election for its trades or businesses, the taxpayer must attach to its tax return a statement identifying and describing the trade or business for which the election is being made, and must provide other information as the Commissioner may require in forms, instructions, or other published guidance. The election is not required. The election is potentially beneficial to businesses with business interest, but is detrimental to businesses that have assets for which bonus depreciation is desired.

The reporting burden is estimated at 0–30 minutes, depending on individual circumstances, with an estimated average of 0.25 hours for all affected entities, regardless of size. The burden on small entities is expected to be the same as other entities because the requirements to make the election apply equally to all taxpayers. Using the IRS's taxpayer compliance cost estimates, the monetization rate is $95 per hour. Thus, the average annual burden is $23.75 per business.

For the section 163(j)(10) elections under §§ 1.163(j)–2(b)(ii) or 1.163(j)–2(b)(3), most small business taxpayers do not need the elections because, as discussed earlier, they are not subject to the section 163(j) limitation. For small taxpayers that are subject to the limitation, the cost to implement the elections is low. Pursuant to Revenue Procedure 2020–22, these taxpayers simply complete the Form 8990 as if the election has been made. Accordingly, the burden of complying with the elections, if needed, is no different than for taxpayers that do not make the elections.

Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding this regulation was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its effect on small business, and no comments were received.

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 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 section, of $100 million in 1995 dollars, update annually for inflation. This rule does not include any Federal mandate that may result in expenditures by state, local, or tribal governments, or by the private section 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 final rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of the Executive Order.

VI. 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 (5 U.S.C. 801 *et seq.*) (CRA). Under section 801(3) of the CRA, a major rule takes effect 60 days after the rule is published in the **Federal Register**. Notwithstanding this requirement, section 808(2) of the CRA allows agencies to dispense with the requirements of 801 when the agency for good cause finds that such procedure would be impracticable, unnecessary, or contrary to the public interest and the rule shall take effect at such time as the agency promulgating the rule determines.

The Treasury Department and the IRS have determined that the rules in this Treasury decision shall take effect for taxable years beginning on or after November 13, 2020. Pursuant to section 808(2) of the CRA, however, the Treasury Department and the IRS find, for good cause, that a 60-day delay in the effective and the applicability date for the anti-avoidance rules in § 1.163(j)–1(b)(22)(iv) is unnecessary and contrary to the public interest. Section 1.163(j)–1(b)(22)(iv) serves an anti-abuse function and, because § 1.163(j)–1(b)(22)(iv) provides a clear scope of abusive transactions that could otherwise be executed prior to the effective date of the section, immediate application of § 1.163(j)–1(b)(22)(iv) is necessary as of the publication of this final regulation.

Drafting Information

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List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

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:

■ 1. Adding entries in numerical order for §§ 1.163(j)–1 through 1.163(j)–11;

■ 2. Revising the entries for §§ 1.263A–8 through 1.263A–15;

■ 3. Adding entries in numerical order for §§ 1.382–1 and 1.383–0;

■ 4. Revising the entry for § 1.383–1; and

■ 5. Adding entries in numerical order for §§ 1.860C–2 and 1.1502–90.

The additions and revisions read as follows:

Authority: 26 U.S.C. 7805, unless otherwise noted.

* * * * *

Section 1.163(j)–1 also issued under 26 U.S.C. 163(j)(8)(B) and 26 U.S.C. 1502.

Section 1.163(j)–2 also issued under 26 U.S.C. 1502.

Section 1.163(j)–3 also issued under 26 U.S.C. 1502.

Section 1.163(j)–4 also issued under 26 U.S.C. 163(j)(8)(B) and 26 U.S.C. 1502.

Section 1.163(j)–5 also issued under 26 U.S.C. 1502.

Section 1.163(j)–6 also issued under 26 U.S.C. 163(j)(8)(B) and 26 U.S.C. 1502.

Section 1.163(j)–7 also issued under 26 U.S.C. 163(j)(8)(B) and 26 U.S.C. 1502.

Section 1.163(j)–8 also issued under 26 U.S.C. 163(j)(8)(B).

Section 1.163(j)–9 also issued under 26 U.S.C. 163(j)(7)(B) and (C) and 26 U.S.C. 1502.

Section 1.163(j)–10 also issued under 26 U.S.C. 163(j)(8)(B) and 26 U.S.C. 1502.

Section 1.163(j)–11 also issued under 26 U.S.C. 1502.

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Sections 1.263A–8 through 1.263A–15 also issued under 26 U.S.C. 263A(j).

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Section 1.382–1 also issued under 26 U.S.C. 382(m).

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Section 1.383–0 also issued under 26 U.S.C. 382(m) and 26 U.S.C. 383.

Section 1.383–1 also issued under 26 U.S.C. 382(m) and 26 U.S.C. 383.

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Section 1.860C–2 also issued under 26 U.S.C. 860C(b)(1) and 860G(e).

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Section 1.1502–90 also issued under 26 U.S.C. 382(m) and 26 U.S.C. 1502.

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■ **Par. 2.** Section 1.163(j)–0 is added to read as follows:

§ 1.163(j)–0 Table of contents.

This section lists the table of contents for §§ 1.163(j)–1 through 1.163(j)–11.

§ 1.163(j)–1 Definitions.

(a) In general.
(b) Definitions.
(1) Adjusted taxable income.
(i) Additions.
(ii) Subtractions.
(iii) Depreciation, amortization, or depletion capitalized under section 263A.
(iv) Application of § 1.163(j)–1(b)(1)(ii)(C), (D), and (E).
(A) Sale or other disposition.
(*1*) In general.
(*2*) Intercompany transactions.
(*3*) Deconsolidations.
(B) Deductions by members of a consolidated group.
(C) Successor assets.
(D) Anti-duplication rule.
(*1*) In general.
(*2*) Adjustments following deconsolidation.
(v) Other adjustments.
(vi) Additional rules relating to adjusted taxable income in other sections.
(vii) ATI cannot be less than zero.
(viii) Examples.
(2) Applicable CFC.
(3) Business interest expense.
(i) In general.
(ii) Special rules.
(4) Business interest income.
(i) In general.
(ii) Special rules.
(5) C corporation.
(6) Cleared swap.
(7) Consolidated group.
(8) Consolidated return year.
(9) Current-year business interest expense.
(10) Disallowed business interest expense.
(11) Disallowed business interest expense carryforward.
(12) Disallowed disqualified interest.
(13) Electing farming business.
(14) Electing real property trade or business.
(15) Excepted regulated utility trade or business.
(i) In general.
(A) Automatically excepted regulated utility trades or businesses.
(B) Electing regulated utility trades or businesses.
(C) Designated excepted regulated utility trades or businesses.
(ii) Depreciation and excepted and non-excepted utility trades or businesses.
(A) Depreciation.
(B) Allocation of items.
(iii) Election to be an excepted regulated utility trade or business.
(A) In general.
(B) Scope and effect of election.
(*1*) In general.
(*2*) Irrevocability.
(C) Time and manner of making election.
(*1*) In general.
(*2*) Election statement contents.
(*3*) Consolidated group's or partnership's trade or business.
(*4*) Termination of election.
(*5*) Additional guidance.
(16) Excess business interest expense.
(17) Excess taxable income.
(18) Floor plan financing indebtedness.
(19) Floor plan financing interest expense.
(20) Group.
(21) Intercompany transaction.
(22) Interest.
(i) In general.
(ii) Swaps with significant nonperiodic payments.
(A) In general.
(B) Exception for cleared swaps.

(C) Exception for non-cleared swaps subject to margin or collateral requirements.
(iii) Other amounts treated as interest.
(A) Treatment of premium.
(*1*) Issuer.
(*2*) Holder.
(B) Treatment of ordinary income or loss on certain debt instruments.
(C) Substitute interest payments.
(D) Section 1258 gain.
(E) Factoring income.
(F) [Reserved]
(iv) Anti-avoidance rules.
(A) Principal purpose to reduce interest expense.
(*1*) Treatment as interest expense.
(*2*) Corresponding treatment of amounts as interest income.
(B) Interest income artificially increased.
(C) Principal purpose.
(D) Coordination with anti-avoidance rule in § 1.163(j)–2(j).
(v) Examples.
(23) Interest expense.
(24) Interest income.
(25) Member.
(26) Motor vehicle.
(27) Old section 163(j).
(28) Ownership change.
(29) Ownership date.
(30) Real estate investment trust.
(31) Real property.
(32) Regulated investment company.
(33) Relevant foreign corporation.
(34) S corporation.
(35) [Reserved]
(36) Section 163(j) limitation.
(37) Section 163(j) regulations.
(38) Separate return limitation year.
(39) Separate return year.
(40) Separate tentative taxable income.
(41) Tax-exempt corporation.
(42) Tax-exempt organization.
(43) Tentative taxable income.
(i) In general.
(ii) [Reserved]
(iii) Special rules for defining tentative taxable income.
(44) Trade or business.
(i) In general.
(ii) Excepted trade or business.
(iii) Non-excepted trade or business.
(45) Unadjusted basis.
(46) United States shareholder.
(c) Applicability date.
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(2) Anti-avoidance rules.
(3) Swaps with significant nonperiodic payments.
(i) In general.
(ii) Anti-avoidance rule.
§ 1.163(j)–2 Deduction for business interest expense limited.
(a) Overview.
(b) General rule.
(1) In general.
(2) 50 percent ATI limitation for taxable years beginning in 2019 or 2020.
(3) Election to use 2019 ATI in 2020.
(4) Time and manner of making or revoking the elections.
(c) Disallowed business interest expense carryforward.
(1) In general.
(2) Coordination with small business exemption.
(3) Cross-references.
(d) Small business exemption.
(1) Exemption.
(2) Application of the gross receipts test.
(i) In general.
(ii) Gross receipts of individuals.
(iii) Partners and S corporation shareholders.
(iv) Tax-exempt organizations.
(e) REMICs.
(f) Trusts.
(i) Calculation of ATI with respect to certain trusts and estates.
(ii) Calculation of ATI with respect to certain beneficiaries.
(g) Tax-exempt organizations.
(h) Examples.
(i) [Reserved]
(j) Anti-avoidance rule.
(1) In general.
(2) Examples.
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(2) Character of deductible business interest expense.
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(4) Adjusted taxable income and business interest income of S corporation shareholders.
(i) Adjusted taxable income of S corporation shareholders.
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(7) Accumulated adjustment accounts.
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(4) REIT real property assets, interests in partnerships, and shares in other REITs.
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(iii) Shares in other REITs.
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§ 1.163(j)–10 Allocation of interest expense, interest income, and other items of expense and gross income to an excepted trade or business.

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(1) In general.
(i) Purposes.
(ii) Application of section.
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(i) In general.
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(3) Application of allocation rules to foreign corporations and foreign partnerships.
(4) Application of allocation rules to members of a consolidated group.
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(ii) Application of excepted business percentage to members of a consolidated group.
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(b) Allocation of tax items other than interest expense and interest income.
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(i) Expenses, losses, and other deductions that are definitely related to a trade or business.
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(i) In general.
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(A) Consistent allocation methodologies.
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(*3*) De minimis rule for excepted utility trades or businesses.
(*4*) Example.
(D) Special allocation rule for real property trades or business subject to special anti-abuse rule.
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(5) Additional rules relating to basis.
(i) Calculation of adjusted basis.
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(B) Depreciable property other than inherently permanent structures.
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(A) Partnership interests.
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(*2*) Allocation of asset basis.
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(*ii*) De minimis rule.
(*iii*) Partnership assets not properly allocable to a trade or business.
(*iv*) Inapplicability of partnership look-through rule.
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(*1*) In general.
(*2*) Domestic non-consolidated C corporations.
(*i*) Allocation of asset basis.
(*ii*) De minimis rule.
(*iii*) Inapplicability of corporate look-through rule.
(*iv*) Use of inside basis for purposes of C corporation look-through rule.
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(*i*) Calculation of asset basis.
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(*1*) In general.
(*2*) Special rule for CFC utilities.
(D) Inapplicability of look-through rule to partnerships or non-consolidated

C corporations to which the small business exemption applies.
(E) Tiered entities.
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(A) Books and records.
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(A) Asset basis.
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(1) In general.
(2) Qualified nonrecourse indebtedness.
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(5) Example: Direct allocation of interest expense.
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§ 1.163(j)–11 Transition rules.
(a) Overview.
(b) Application of section 163(j) limitation if a corporation joins a consolidated group during a taxable year of the group beginning before January 1, 2018.
(1) In general.
(2) Example
(c) Treatment of disallowed disqualified interest.
(1) In general.
(2) Earnings and profits.
(3) Disallowed disqualified interest of members of an affiliated group.
(i) Scope.
(ii) Allocation of disallowed disqualified interest to members of the affiliated group.
(A) In general.
(B) Definitions.
(*1*) Allocable share of the affiliated group's disallowed disqualified interest.
(*2*) Disallowed disqualified interest ratio.
(*3*) Exempt related person interest expense.
(iii) Treatment of carryforwards.
(4) Application of section 382.
(i) Ownership change occurring before November 13, 2020.
(A) Pre-change loss.
(B) Loss corporation.
(ii) Ownership change occurring on or after November 13, 2020.
(A) Pre-change loss.
(B) Loss corporation.
(5) Treatment of excess limitation from taxable years beginning before January 1, 2018.
(6) Example: Members of an affiliated group.
(d) Applicability date.

■ **Par. 3.** Sections 1.163(j)–1 through 1.163(j)–11 are added to read as follows:

Sec.
* * * * *
1.163(j)–1 Definitions.
1.163(j)–2 Deduction for business interest expense limited.
1.163(j)–3 Relationship of the section 163(j) limitation to other provisions affecting interest.
1.163(j)–4 General rules applicable to C corporations (including REITs, RICs, and members of consolidated groups) and tax-exempt corporations.
1.163(j)–5 General rules governing disallowed business interest expense carryforwards for C corporations.
1.163(j)–6 Application of the section 163(j) limitation to partnerships and subchapter S corporations.
1.163(j)–7 Application of the section 163(j) limitation to foreign corporations and United States shareholders.
1.163(j)–8 [Reserved]
1.163(j)–9 Elections for excepted trades or businesses; safe harbor for certain REITs.
1.163(j)–10 Allocation of interest expense, interest income, and other items of expense and gross income to an excepted trade or business.
1.163(j)–11 Transition rules.
* * * * *

§ 1.163(j)–1 Definitions.

(a) *In general.* The definitions provided in this section apply for purposes of the section 163(j) regulations. For purposes of the rules set forth in §§ 1.163(j)–2 through 1.163(j)–11, additional definitions for certain terms are provided in those sections.

(b) *Definitions*—(1) *Adjusted taxable income.* The term *adjusted taxable income* (ATI) means the tentative taxable income of the taxpayer for the taxable year, with the adjustments in this paragraph (b)(1).

(i) *Additions.* The amounts of the following items that were included in the computation of the taxpayer's tentative taxable income (if any) are added to tentative taxable income to determine ATI—

(A) Any business interest expense, other than disallowed business interest expense carryforwards;

(B) Any net operating loss deduction under section 172;

(C) Any deduction under section 199A;

(D) Subject to paragraph (b)(1)(iii) of this section, for taxable years beginning before January 1, 2022, any depreciation under section 167, section 168, or section 168 of the Internal Revenue Code (Code) of 1954 (former section 168);

(E) Subject to paragraph (b)(1)(iii) of this section, for taxable years beginning before January 1, 2022, any amortization of intangibles (for example, under section 167 or 197) and other amortized expenditures (for example, under section 174(b), 195(b)(1)(B), 248, or 1245(a)(2)(C));

(F) Subject to paragraph (b)(1)(iii) of this section, for taxable years beginning before January 1, 2022, any depletion under section 611;

(G) Any deduction for a capital loss carryback or carryover; and

(H) Any deduction or loss that is not properly allocable to a non-excepted trade or business (for rules governing the allocation of items to an excepted trade or business, see §§ 1.163(j)–1(b)(44) and 1.163(j)–10).

(ii) *Subtractions.* The amounts of the following items (if any) are subtracted from the taxpayer's tentative taxable income to determine ATI —

(A) Any business interest income that was included in the computation of the taxpayer's tentative taxable income;

(B) Any floor plan financing interest expense for the taxable year that was included in the computation of the taxpayer's tentative taxable income;

(C) With respect to the sale or other disposition of property, the greater of the allowed or allowable depreciation, amortization, or depletion of the property, as provided under section 1016(a)(2), for the taxpayer (or, if the taxpayer is a member of a consolidated group, the consolidated group) for the taxable years beginning after December 31, 2017, and before January 1, 2022, with respect to such property;

(D) With respect to the sale or other disposition of stock of a member of a consolidated group by another member, the investment adjustments under § 1.1502–32 with respect to such stock that are attributable to deductions described in paragraph (b)(1)(ii)(C) of this section;

(E) With respect to the sale or other disposition of an interest in a partnership, the taxpayer's distributive share of deductions described in paragraph (b)(1)(ii)(C) of this section with respect to property held by the partnership at the time of such sale or other disposition to the extent such deductions were allowable under section 704(d);

(F) Any income or gain that is not properly allocable to a non-excepted trade or business (for rules governing the allocation of items to an excepted trade or business, see §§ 1.163(j)–1(b)(44) and 1.163(j)–10)) and that was included in the computation of the taxpayer's tentative taxable income; and

(G) An amount equal to the sum of any specified deemed inclusions that were included in the computation of the taxpayer's tentative taxable income, reduced by the portion of the deduction allowed under section 250(a) by reason of the specified deemed inclusions. For this purpose, a *specified deemed inclusion* is the inclusion of an amount by a United States shareholder (as defined in section 951(b)) in gross income under section 78, 951(a), or 951A(a) with respect to an applicable CFC (as defined in § 1.163(j)–1(b)(2)) that is properly allocable to a non-excepted trade or business. Furthermore, a specified deemed inclusion includes any amounts included in a domestic partnership's gross income under section 951(a) or 951A(a) with respect to an applicable CFC to the extent such amounts are attributable to investment income of the partnership and are allocated to a domestic C corporation that is a direct (or indirect partner) and treated as properly allocable to a non-excepted trade or business of the domestic C corporation under §§ 1.163(j)–4(b)(3) and 1.163(j)–10. To determine the amount of a specified deemed inclusion described in this paragraph (b)(1)(ii)(G), the portion of a United States shareholder's inclusion under section 951A(a) treated as being with respect to an applicable CFC is determined under section 951A(f)(2) and § 1.951A–6(b)(2).

(iii) *Depreciation, amortization, or depletion capitalized under section 263A.* For purposes of paragraph (b)(1)(i) of this section, amounts of depreciation, amortization, or depletion that are capitalized under section 263A during the taxable year are deemed to be included in the computation of the taxpayer's tentative taxable income for such taxable year, regardless of the period in which the capitalized amount is recovered. See *Example 3* in § 1.163(j)–2(h)(3).

(iv) *Application of § 1.163(j)–1(b)(1)(ii)(C), (D), and (E)*—(A) *Sale or other disposition*—(*1*) *In general.* For purposes of paragraphs (b)(1)(ii)(C), (D), and (E) of this section, except as otherwise provided in this paragraph (b)(1)(iv)(A), the term *sale or other disposition* does not include a transfer of an asset to an acquiring corporation in a transaction to which section 381(a) applies.

(*2*) *Intercompany transactions.* For purposes of paragraphs (b)(1)(ii)(C) and (D) of this section, the term *sale or other disposition* excludes all intercompany transactions, within the meaning of § 1.1502–13(b)(1)(i).

(*3*) *Deconsolidations.* Notwithstanding any other rule in this paragraph (b)(1)(iv)(A), any transaction in which a member leaves a consolidated group is treated as a sale or other disposition for purposes of paragraphs (b)(1)(ii)(C) and (D) of this section unless the transaction is described in § 1.1502–13(j)(5)(i)(A).

(B) *Deductions by members of a consolidated group.* If paragraph (b)(1)(ii)(C), (D), or (E) of this section applies to adjust the tentative taxable income of a taxpayer, the amount of the adjustment under paragraph (b)(1)(ii)(C) of this section equals the greater of the allowed or allowable depreciation, amortization, or depletion of the property, as provided under section 1016(a)(2), for any member of the consolidated group for the taxable years beginning after December 31, 2017, and before January 1, 2022, with respect to such property.

(C) *Successor assets.* This paragraph (b)(1)(iv)(C) applies if deductions described in paragraph (b)(1)(ii)(C) of this section are allowed or allowable to a consolidated group member (S) and either the depreciable property or S's stock is subsequently transferred to another member (S1) in an intercompany transaction in which the transferor receives S1 stock. If this paragraph (b)(1)(iv)(C) applies, and if the transferor's basis in the S1 stock received in the intercompany transaction is determined, in whole or in part, by reference to its basis in the S stock, the S1 stock received in the intercompany transaction is treated as a successor asset to S's stock for purposes of paragraph (b)(1)(ii)(D) of this section. Thus, except as otherwise provided in paragraph (b)(1)(iv)(D) of this section, the subsequent disposition of either the S1 stock or the S stock gives rise to an adjustment under paragraph (b)(1)(ii)(D) of this section.

(D) *Anti-duplication rule*—(*1*) *In general.* The aggregate of the subtractions from tentative taxable income of a consolidated group under paragraphs (b)(1)(ii)(C) and (D) of this section with respect to an item of property (including with regard to dispositions of successor assets described in paragraph (b)(1)(iv)(C) of this section) cannot exceed the aggregate amount of the consolidated group members' deductions described in paragraph (b)(1)(ii)(C) of this section with respect to such item of property. For example, if an adjustment to the tentative taxable income of a consolidated group is made under paragraph (b)(1)(ii)(C) of this section with respect to the sale or other disposition of property by a consolidated group member (S) to an unrelated person, and if a member of the group subsequently sells or otherwise disposes of S's stock, no further adjustment to the group's tentative taxable income is made under paragraph (b)(1)(ii)(D) of this section in relation to the same property with respect to that stock disposition.

(*2*) *Adjustments following deconsolidation.* Depreciation, amortization, or depletion deductions allowed or allowable for a corporation for a consolidated return year of a group are disregarded in applying this paragraph (b)(1)(iv)(D) to any year that constitutes a separate return year (as defined in § 1.1502–1(e)) of that corporation. For example, assume that S deconsolidates from a group (Group 1) after holding property for which depreciation, amortization, or depletion deductions were allowed or allowable in Group 1. On the deconsolidation, S and Group 1 would adjust tentative taxable income with regard to that property under paragraphs (b)(1)(ii)(D) and (b)(1)(iv)(A)(*3*) of this section. If, following the deconsolidation, S sells the property referred to in the previous sentence, no subtraction from tentative taxable income is made under paragraph (b)(1)(ii)(C) of this section during S's separate return year with regard to the amounts included in Group 1 under paragraphs (b)(1)(ii)(C) and (b)(1)(iv)(A)(*3*) of this section.

(v) *Other adjustments.* ATI is computed with the other adjustments provided in §§ 1.163(j)–2 through 1.163(j)–11.

(vi) *Additional rules relating to adjusted taxable income in other sections.* (A) For rules governing the ATI of C corporations, see §§ 1.163(j)–4(b)(2) and (3) and 1.163(j)–10(a)(2)(ii).

(B) For rules governing the ATI of RICs and REITs, see § 1.163(j)–4(b)(4).

(C) For rules governing the ATI of tax-exempt corporations, see § 1.163(j)–4(b)(5).

(D) For rules governing the ATI of consolidated groups, see § 1.163(j)–4(d)(2)(iv) and (v).

(E) For rules governing the ATI of partnerships, see § 1.163(j)–6(d).

(F) For rules governing the ATI of partners, see §§ 1.163(j)–6(e) and 1.163(j)–6(m)(1) and (2).

(G) For rules governing partnership basis adjustments affecting ATI, see § 1.163(j)–6(h)(2).

(H) For rules governing the ATI of S corporations, see § 1.163(j)–6(l)(3).

(I) For rules governing the ATI of S corporation shareholders, see § 1.163(j)–6(l)(4).

(J) For rules governing the ATI of certain beneficiaries of trusts and estates, see § 1.163(j)–2(f).

(vii) *ATI cannot be less than zero.* If the ATI of a taxpayer would be less than zero, the ATI of the taxpayer is zero.

(viii) *Examples.* The examples in this paragraph (b)(1)(viii) illustrate the application of paragraphs (b)(1)(ii), (iii), and (iv) of this section. Unless otherwise indicated, A, B, P, S, and T are calendar-year domestic C corporations; P is the parent of a consolidated group of which S and T are members; the exemption for certain small businesses in § 1.163(j)–2(d) does not apply; no entity is engaged in an excepted trade or business; no entity has business interest income or floor plan financing interest expense; and all amounts of interest expense are deductible except for the potential application of section 163(j).

(A) *Example 1*—(*1*) *Facts.* In 2021, A purchases a depreciable asset (Asset X) for $100x and fully depreciates Asset X under section 168(k). For the 2021 taxable year, A's ATI (after adding back A's depreciation deductions with respect to Asset X under paragraph (b)(1)(i)(D) of this section) is $150x. A incurs $45x of business interest expense in 2021. In 2024, A sells Asset X to an unrelated third party.

(*2*) *Analysis.* A's section 163(j) limitation for 2021 is $45x ($150x × 30 percent). Thus, all $45x of A's business interest expense incurred in 2021 is deductible in that year. However, under paragraph (b)(1)(ii)(C) of this section, A must subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year. A would be required to subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year even if A's ATI in 2021 was $150x before adding back A's depreciation deductions with respect to Asset X.

(*3*) *Transfer of assets in a nonrecognition transaction to which section 381 applies.* The facts are the same as in paragraph (b)(1)(viii)(A)(*1*) of this section, except that, rather than sell Asset X to an unrelated third party in 2024, A merges with and into an unrelated third party in 2024 in a transaction described in section 368(a)(1)(A) in which no gain is recognized. As provided in paragraph (b)(1)(iv)(A) of this section, the merger transaction is not treated as a ''sale or other disposition'' for purposes of paragraph (b)(1)(ii)(C) of this section. Thus, no adjustment to tentative taxable income is required in 2024 under paragraph (b)(1)(ii)(C) of this section.

(*4*) *Transfer of assets in a nonrecognition transaction to which section 351 applies.* The facts are the same as in paragraph (b)(1)(viii)(A)(*1*) of this section, except that, rather than sell Asset X to an unrelated third party in 2024, A transfers Asset X to B (A's wholly owned subsidiary) in 2024 in a transaction to which section 351 applies. The section 351 transaction is treated as a ''sale or other disposition'' for purposes of paragraph (b)(1)(ii)(C) of this section. Thus, A must subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year.

(B) *Example 2*—(*1*) *Facts.* In 2021, S purchases a depreciable asset (Asset Y) for $100x and fully depreciates Asset Y under section 168(k). P reduces its basis in its S stock by $100x under § 1.1502–32 to reflect S's depreciation deductions. For the 2021 taxable year, the P group's ATI (after adding back S's depreciation deductions with respect to Asset Y under paragraph (b)(1)(i)(D) of this section) is $150x. The P group incurs $45x of business interest expense in 2021. In 2024, P sells all of its S stock to an unrelated third party.

(*2*) *Analysis.* The P group's section 163(j) limitation for 2021 is $45x ($150x × 30 percent). Thus, all $45x of the P group's business interest expense incurred in 2021 is deductible in that year. However, under paragraph (b)(1)(ii)(D) of this section, the P group must subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year. The answer would be the same if the P group's ATI in 2021 were $150x before adding back S's depreciation deductions with respect to Asset Y.

(*3*) *Disposition of less than all member stock.* The facts are the same as in paragraph (b)(1)(viii)(B)(*1*) of this section, except that, in 2024, P sells half of its S stock to an unrelated third party. Pursuant to paragraph (b)(1)(ii)(D) of this section, the P group must subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year.

(*4*) *Transfer in an intercompany transaction.* The facts are the same as in paragraph (b)(1)(viii)(B)(*1*) of this section, except that, rather than sell S's stock to an unrelated third party in 2024, P transfers S's stock to another member of the P group in an intercompany transaction (as defined in § 1.1502–13(b)(1)(i)) in 2024. As provided in paragraph (b)(1)(iv)(A) of this section, the intercompany transaction is not treated as a ''sale or other disposition'' for purposes of paragraph (b)(1)(ii)(D) of this section. Thus, no adjustment to tentative taxable income is required in 2024 under paragraph (b)(1)(ii)(D) of this section.

(*5*) *Disposition of successor assets.* The facts are the same as in paragraph (b)(1)(viii)(B)(*1*) of this section, except that, rather than sell S's stock to an unrelated third party in 2024, P transfers S's stock to T in 2024 in a transaction to which section 351 applies and, in 2025, P sells all of its T stock to an unrelated third party. Pursuant to paragraph (b)(1)(iv)(A) of this section, P's intercompany transfer of S's stock to T is not a ''sale or other disposition'' for purposes of paragraph (b)(1)(ii)(D) of this section. However, pursuant to paragraph (b)(1)(iv)(C) of this section, P's stock in T is treated as a successor asset for purposes of paragraph (b)(1)(ii)(D) of this section. Thus, the P group must subtract $100x from its tentative taxable income in computing its ATI for its 2025 taxable year.

(C) *Example 3*—(*1*) *Facts.* In 2021, S purchases a depreciable asset (Asset Z) for $100x and fully depreciates Asset Z under section 168(k). P reduces its basis in its S stock by $100x under § 1.1502–32 to reflect S's depreciation deductions. For the 2021 taxable year, the P group's ATI (after adding back S's depreciation deductions with respect to Asset Z under paragraph (b)(1)(i)(D) of this section) is $150x. The P group incurs $45x of business interest expense in 2021. In 2024, S sells Asset Z to an unrelated third party. In 2025, P sells all of its S stock to a member of another consolidated group.

(*2*) *Analysis.* Under paragraph (b)(1)(ii)(C) of this section, the P group must subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year. The answer would be the same if the P group's ATI in 2021 were $150x before adding back S's depreciation deductions with respect to Asset Z. P's sale of all of its S stock in 2025 is a ''sale or other disposition'' for purposes of paragraph (b)(1)(ii)(D) of this section. However, pursuant to paragraph (b)(1)(iv)(D)(*1*) of this section, no further adjustment to the P group's tentative taxable income is required in 2025 under paragraph (b)(1)(ii)(D) of this section.

(*3*) *Disposition of S stock prior to S's asset disposition.* The facts are the same as in paragraph (b)(1)(viii)(C)(*1*) of this section, except that, in 2024, P sells all of its S stock to a member of another consolidated group and, in 2025, S sells Asset Z to an unrelated third party. Pursuant to paragraph (b)(1)(ii)(D) of this section, the P group must subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year. Pursuant to paragraph (b)(1)(iv)(D)(*2*) of this section, no adjustment to the acquiring group's tentative taxable income is required in 2025 under paragraph (b)(1)(ii)(C) of this section.

(*4*) *Transfer of S stock in nonrecognition transaction.* The facts are the same as in paragraph (b)(1)(vii)(C)(*3*) of this section, except that, rather than sell all of S's stock to a member of another consolidated group, P causes S to merge with and into a member of another consolidated group in a transaction described in section 368(a)(1)(A). As provided in paragraph (b)(1)(iv)(A) of this section, the merger transaction is treated as a ''sale or other disposition'' for purposes of paragraph (b)(1)(ii)(D) of this section because S leaves the P group. Thus, the results are the same as in paragraph (b)(1)(vii)(C)(*3*) of this section.

(D) *Example 4*—(*1*) *Facts.* P wholly owns T, which wholly owns S. In 2021, S purchases a depreciable asset (Asset AA) for $100x and fully depreciates Asset AA under section 168(k). T reduces its basis in its S stock, and P reduces its basis in its T stock, by $100x under § 1.1502–32 to reflect S's depreciation deductions. For the 2021 taxable year, the P group's ATI (after adding back S's depreciation deductions with respect to Asset AA under paragraph (b)(1)(i)(D) of this section) is $150x. The P group incurs $45x of business interest expense in 2021. In 2024, T sells all of its S stock to a member of another consolidated group. In 2025, P sells all of its T stock to a member of another consolidated group.

(*2*) *Analysis.* Pursuant to paragraph (b)(1)(ii)(D) of this section, the P group must subtract $100x from its tentative taxable income in computing its ATI for its 2024 taxable year. Pursuant to paragraph (b)(1)(iv)(D)(*1*) of this section, no adjustment to the P group's tentative taxable income is required in 2025 under paragraph (b)(1)(ii)(D) of this section.

(2) *Applicable CFC.* The term *applicable CFC* means a foreign corporation described in section 957, but only if the foreign corporation has at least one United States shareholder that owns, within the meaning of section 958(a), stock of the foreign corporation.

(3) *Business interest expense*—(i) *In general.* The term *business interest expense* means interest expense that is properly allocable to a non-excepted trade or business or that is floor plan financing interest expense. Business interest expense also includes disallowed business interest expense carryforwards (as defined in paragraph (b)(11) of this section). However, business interest expense does not include amounts of interest expense carried forward to the taxable year from a prior taxable year due to the application of section 465 or section 469, which apply after the application of section 163(j). For the treatment of investment interest, see section 163(d); and for the treatment of personal interest, see section 163(h).

(ii) *Special rules.* For special rules for defining business interest expense in certain circumstances, see §§ 1.163(j)–3(b)(2) (regarding disallowed interest expense), 1.163(j)–4(b) (regarding C corporations) and 1.163(j)–4(d)(2)(iii) (regarding consolidated groups), 1.163(j)–1(b)(9) (regarding current-year business interest expense), and 1.163(j)–6(c) (regarding partnerships and S corporations).

(4) *Business interest income*—(i) *In general.* The term *business interest income* means interest income includible in the gross income of a taxpayer for the taxable year which is properly allocable to a non-excepted trade or business. For the treatment of investment income, see section 163(d).

(ii) *Special rules.* For special rules defining business interest income in certain circumstances, see §§ 1.163(j)–4(b) (regarding C corporations), 1.163(j)–4(d)(2)(iii) (regarding consolidated groups), and 1.163(j)–6(c) (regarding partnerships and S corporations).

(5) *C corporation.* The term *C corporation* has the meaning provided in section 1361(a)(2).

(6) *Cleared swap.* The term *cleared swap* means a swap that is cleared by a derivatives clearing organization, as such term is defined in section 1a of the Commodity Exchange Act (7 U.S.C. 1a), or by a clearing agency, as such term is defined in section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c), that is registered as a derivatives clearing organization under the Commodity Exchange Act or as a clearing agency under the Securities Exchange Act of 1934, respectively, if the derivatives clearing organization or clearing agency requires the parties to the swap to post and collect margin or collateral.

(7) *Consolidated group.* The term *consolidated group* has the meaning provided in § 1.1502–1(h).

(8) *Consolidated return year.* The term *consolidated return year* has the meaning provided in § 1.1502–1(d).

(9) *Current-year business interest expense.* The term *current-year business interest expense* means business interest expense that would be deductible in the current taxable year without regard to section 163(j) and that is not a disallowed business interest expense carryforward from a prior taxable year.

(10) *Disallowed business interest expense.* The term *disallowed business interest expense* means the amount of business interest expense for a taxable year in excess of the amount allowed as a deduction for the taxable year under section 163(j)(1) and § 1.163(j)–2(b). For purposes of section 163(j) and the regulations in this part under section 163(j) of the Internal Revenue Code (Code) disallowed business interest expense is treated as ''paid or accrued'' in the taxable year in which the expense is deductible for Federal income tax purposes (without regard to section 163(j)) or in the taxable year in which a deduction for the business interest expense is permitted under section 163(j), as the context may require.

(11) *Disallowed business interest expense carryforward.* The term *disallowed business interest expense carryforward* means any business interest expense described in § 1.163(j)–2(c).

(12) *Disallowed disqualified interest.* The term *disallowed disqualified interest* means interest expense, including carryforwards, for which a deduction was disallowed under old section 163(j) (as defined in paragraph (b)(27) of this section) in the taxpayer's last taxable year beginning before January 1, 2018, and that was carried forward pursuant to old section 163(j).

(13) *Electing farming business.* The term *electing farming business* means a trade or business that makes an election as provided in § 1.163(j)–9 or other published guidance and that is—

(i) A farming business, as defined in section 263A(e)(4) or § 1.263A–4(a)(4);

(ii) Any trade or business of a specified agricultural or horticultural cooperative, as defined in section 199A(g)(4); or

(iii) Specifically designated by the Secretary in guidance published in the **Federal Register** or the Internal Revenue Bulletin (see § 601.601(d) of this chapter) as a farming business for purposes of section 163(j).

(14) *Electing real property trade or business.* The term *electing real property trade or business* means a trade or business that makes an election as provided in § 1.163(j)–9 or other published guidance and that is—

(i) A real property trade or business described in section 469(c)(7)(C) and § 1.469–9(b)(2); or

(ii) A REIT that qualifies for the safe harbor described in § 1.163(j)–9(h); or

(iii) A trade or business specifically designated by the Secretary in guidance published in the **Federal Register** or the

Internal Revenue Bulletin (see § 601.601(d) of this chapter) as a real property trade or business for purposes of section 163(j).

(15) *Excepted regulated utility trade or business*—(i) *In general.* The term *excepted regulated utility trade or business* means:

(A) *Automatically excepted regulated utility trades or businesses.* A trade or business—

(*1*) That furnishes or sells—

(*i*) Electrical energy, water, or sewage disposal services;

(*ii*) Gas or steam through a local distribution system; or

(*iii*) Transportation of gas or steam by pipeline; but only

(*2*) To the extent that the rates for the furnishing or sale of the items in paragraph (b)(15)(i)(A)(*1*) of this section—

(*i*) Have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof and are determined on a cost of service and rate of return basis; or

(*ii*) Have been established or approved by the governing or ratemaking body of an electric cooperative; or

(B) *Electing regulated utility trades or businesses.* A trade or business that makes a valid election under paragraph (b)(15)(iii) of this section; or

(C) *Designated excepted regulated utility trades or businesses.* A trade or business that is specifically designated by the Secretary in guidance published in the **Federal Register** or the Internal Revenue Bulletin as an excepted regulated utility trade or business (see § 601.601(d) of this chapter) for section 163(j) purposes.

(ii) *Depreciation and excepted and non-excepted utility trades or businesses.*

(A) *Depreciation.* Taxpayers engaged in an excepted trade or business described in paragraph (b)(15)(i) of this section cannot claim the additional first-year depreciation deduction under section 168(k) for any property that is primarily used in the excepted regulated utility trade or business.

(B) *Allocation of items.* If a taxpayer is engaged in one or more excepted trades or businesses, as described in paragraph (b)(15)(i) of this section, and one or more non-excepted trades or businesses, the taxpayer must allocate items between the excepted and non-excepted utility trades or businesses. See §§ 1.163(j)–1(b)(44) and 1.163(j)–10(c)(3)(iii)(C). Some trades or businesses with de minimis furnishing or sales of items described in paragraph (b)(15)(i)(A)(*1*) of this section that are not sold pursuant to rates that are determined on a cost of service and rate of return basis or established or approved by the governing or ratemaking body of an electric cooperative, and are not subject to an election in paragraph (b)(15)(iii), are treated as excepted trades or businesses. See § 1.163(j)–10(c)(3)(iii)(C)(*3*). For look-through rules applicable to certain CFCs that furnish or sell items described in paragraph (b)(15)(i)(A)(*1*) of this section that are not sold pursuant to rates that are determined on a cost of service and rate of return basis or established or approved by the governing or ratemaking body of an electric cooperative as described in paragraph (b)(15)(i)(A)(*2*) of this section, see § 1.163(j)–10(c)(5)(ii)(C).

(iii) *Election to be an excepted regulated utility trade or business.* (A) *In general.* A trade or business that is not an excepted regulated utility trade or business described in paragraph (b)(15)(i)(A) or (C) of this section and that furnishes or sells items described in paragraph (b)(15)(i)(A)(*1*) of this section is eligible to make an election to be an excepted regulated utility trade or business to the extent that the rates for furnishing or selling the items described in paragraph (b)(15)(i)(A)(*1*) of this section have been established or approved by a regulatory body described in paragraph (b)(15)(i)(A)(*2*)(i) of this section.

(B) *Scope and effect of election*—(*1*) *In general.* An election under paragraph (b)(15)(iii) of this section is made with respect to each eligible trade or business of the taxpayer and applies only to the trade or business for which the election is made. An election under paragraph (b)(15)(iii) of this section applies to the taxable year in which the election is made and to all subsequent taxable years.

(*2*) *Irrevocability.* An election under paragraph (b)(15)(iii) of this section is irrevocable.

(C) *Time and manner of making election*—(*1*) *In general.* Subject to paragraph (b)(15)(iii)(C)(*5*) of this section, a taxpayer makes an election under paragraph (b)(15)(iii) by attaching an election statement to the taxpayer's timely filed original Federal income tax return, including extensions. A taxpayer may make elections for multiple trades or businesses on a single election statement.

(*2*) *Election statement contents.* The election statement should be titled ''Section 1.163(j)–1(b)(15)(iii) Election'' and must contain the following information for each trade or business:

(*i*) The taxpayer's name;

(*ii*) The taxpayer's address;

(*iii*) The taxpayer's social security number (SSN) or employer identification number (EIN);

(*iv*) A description of the taxpayer's electing trade or business sufficient to demonstrate qualification for an election under this section, including the principal business activity code; and

(*v*) A statement that the taxpayer is making an election under section 1.163(j)–1(b)(15)(iii).

(*3*) *Consolidated group's or partnership's trade or business.* The rules in § 1.163(j)–9(d)(3) and (4) apply with respect to an election under paragraph (b)(15)(iii) of this section for a consolidated group's or partnership's trade or business.

(*4*) *Termination of election.* The rules in § 1.163(j)–9(e) apply to determine when an election under paragraph (b)(15)(iii) of this section terminates.

(*5*) *Additional guidance.* The rules and procedures regarding the time and manner of making an election under paragraph (b)(15)(iii) of this section and the election statement contents in paragraph (b)(15)(iii)(C)(*2*) of this section may be modified through other guidance (see §§ 601.601(d) and 601.602 of this chapter). Additional situations in which an election may terminate under paragraph (b)(15)(iii)(C)(*4*) of this section may be provided through guidance published in the **Federal Register** or in the Internal Revenue Bulletin (see § 601.601(d) of this chapter).

(16) *Excess business interest expense.* For any partnership, the term *excess business interest expense* means the amount of disallowed business interest expense of the partnership for a taxable year under section § 1.163(j)–2(b). With respect to a partner, see § 1.163(j)–6(g) and (h).

(17) *Excess taxable income.* With respect to any partnership or S corporation, the term *excess taxable income* means the amount which bears the same ratio to the partnership's ATI as—

(i) The excess (if any) of—

(A) The amount determined for the partnership or S corporation under section 163(j)(1)(B); over

(B) The amount (if any) by which the business interest expense of the partnership, reduced by the floor plan financing interest expense, exceeds the business interest income of the partnership or S corporation; bears to

(ii) The amount determined for the partnership or S corporation under section 163(j)(1)(B).

(18) *Floor plan financing indebtedness.* The term floor plan

financing indebtedness means indebtedness—

(i) Used to finance the acquisition of motor vehicles held for sale or lease; and

(ii) Secured by the motor vehicles so acquired.

(19) *Floor plan financing interest expense.* The term *floor plan financing interest expense* means interest paid or accrued on floor plan financing indebtedness. For purposes of the section 163(j) regulations, all floor plan financing interest expense is treated as business interest expense. See paragraph (b)(3) of this section.

(20) *Group.* The term *group* has the meaning provided in § 1.1502–1(a).

(21) *Intercompany transaction.* The term *intercompany transaction* has the meaning provided in § 1.1502–13(b)(1)(i).

(22) *Interest.* The term *interest* means any amount described in paragraph (b)(22)(i), (ii), (iii), or (iv) of this section.

(i) *In general.* Interest is an amount paid, received, or accrued as compensation for the use or forbearance of money under the terms of an instrument or contractual arrangement, including a series of transactions, that is treated as a debt instrument for purposes of section 1275(a) and § 1.1275–1(d), and not treated as stock under § 1.385–3, or an amount that is treated as interest under other provisions of the Code or the Income Tax Regulations. Thus, interest includes, but is not limited to, the following:

(A) Original issue discount (OID), as adjusted by the holder for any acquisition premium or amortizable bond premium;

(B) Qualified stated interest, as adjusted by the holder for any amortizable bond premium or by the issuer for any bond issuance premium;

(C) Acquisition discount;

(D) Amounts treated as taxable OID under section 1286 (relating to stripped bonds and stripped coupons);

(E) Accrued market discount on a market discount bond to the extent includible in income by the holder under either section 1276(a) or 1278(b);

(F) OID includible in income by a holder that has made an election under § 1.1272–3 to treat all interest on a debt instrument as OID;

(G) OID on a synthetic debt instrument arising from an integrated transaction under § 1.1275–6;

(H) Repurchase premium to the extent deductible by the issuer under § 1.163–7(c) (determined without regard to section 163(j));

(I) Deferred payments treated as interest under section 483;

(J) Amounts treated as interest under a section 467 rental agreement;

(K) Amounts treated as interest under section 988;

(L) Forgone interest under section 7872;

(M) De minimis OID taken into account by the issuer;

(N) Amounts paid or received in connection with a sale-repurchase agreement treated as indebtedness under Federal tax principles; however, in the case of a sale-repurchase agreement relating to tax-exempt bonds, the amount is not tax-exempt interest;

(O) Redeemable ground rent treated as interest under section 163(c); and

(P) Amounts treated as interest under section 636.

(ii) *Swaps with significant nonperiodic payments*—(A) *In general.* Except as provided in paragraphs (b)(22)(ii)(B) and (C) of this section, a swap with significant nonperiodic payments is treated as two separate transactions consisting of an on-market, level payment swap and a loan. The loan must be accounted for by the parties to the contract independently of the swap. The time value component associated with the loan, determined in accordance with § 1.446–3(f)(2)(iii)(A), is recognized as interest expense to the payor and interest income to the recipient.

(B) *Exception for cleared swaps.* Paragraph (b)(22)(ii)(A) of this section does not apply to a cleared swap (as defined in paragraph (b)(6) of this section).

(C) *Exception for non-cleared swaps subject to margin or collateral requirements.* Paragraph (b)(22)(ii)(A) of this section does not apply to a non-cleared swap that requires the parties to meet the margin or collateral requirements of a federal regulator or that provides for margin or collateral requirements that are substantially similar to a cleared swap or a non-cleared swap subject to the margin or collateral requirements of a federal regulator. For purposes of this paragraph (b)(22)(ii)(C), the term *federal regulator* means the Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), or a prudential regulator, as defined in section 1a(39) of the Commodity Exchange Act (7 U.S.C. 1a), as amended by section 721 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Public Law 111–203, 124 Stat. 1376, Title VII.

(iii) *Other amounts treated as interest*—(A) *Treatment of premium*—(*1*) *Issuer.* If a debt instrument is issued at a premium within the meaning of § 1.163–13, any ordinary income under § 1.163–13(d)(4) is treated as interest income of the issuer.

(*2*) *Holder.* If a taxable debt instrument is acquired at a premium within the meaning of § 1.171–1 and the holder elects to amortize the premium, any amount deductible as a bond premium deduction under section 171(a)(1) and § 1.171–2(a)(4)(i)(A) or (C) is treated as interest expense of the holder.

(B) *Treatment of ordinary income or loss on certain debt instruments.* If an issuer of a contingent payment debt instrument subject to § 1.1275–4(b), a nonfunctional currency contingent payment debt instrument subject to § 1.988–6, or an inflation-indexed debt instrument subject to § 1.1275–7 recognizes ordinary income on the debt instrument in accordance with the rules in § 1.1275–4(b), § 1.988–6(b)(2), or § 1.1275–7(f), whichever is applicable, the ordinary income is treated as interest income of the issuer. If a holder of a contingent payment debt instrument subject to § 1.1275–4(b), a nonfunctional currency contingent payment debt instrument subject to § 1.988–6, or an inflation-indexed debt instrument subject to § 1.1275–7 recognizes an ordinary loss on the debt instrument in accordance with the rules in § 1.1275–4(b), § 1.988–6(b)(2), or § 1.1275–7(f), whichever is applicable, the ordinary loss is treated as interest expense of the holder.

(C) *Substitute interest payments.* A substitute interest payment described in § 1.861–2(a)(7) is treated as interest expense to the payor only if the payment relates to a sale-repurchase agreement or a securities lending transaction that is not entered into by the payor in the ordinary course of the payor's business. A substitute interest payment described in § 1.861–2(a)(7) is treated as interest income to the recipient only if the payment relates to a sale-repurchase agreement or a securities lending transaction that is not entered into by the recipient in the ordinary course of the recipient's business; however, in the case of a sale-repurchase agreement or a securities lending transaction relating to tax-exempt bonds, the recipient of a substitute payment does not receive tax-exempt interest income. This paragraph (b)(22)(iii)(C) does not apply to an amount described in paragraph (b)(22)(i)(N) of this section.

(D) *Section 1258 gain.* Any gain treated as ordinary gain under section 1258 is treated as interest income.

(E) *Factoring income.* The excess of the amount that a taxpayer collects on a factored receivable (or realizes upon the sale or other disposition of the factored receivable) over the amount paid for the factored receivable by the taxpayer is treated as interest income. For purposes of this paragraph (b)(22)(iii)(E), the term *factored receivable* includes any account receivable or other evidence of indebtedness, whether or not issued at a discount and whether or not bearing stated interest, arising out of the disposition of property or the performance of services by any person, if such account receivable or evidence of indebtedness is acquired by a person other than the person who disposed of the property or provided the services that gave rise to the account receivable or evidence of indebtedness. This paragraph (b)(22)(iii)(E) does not apply to an amount described in paragraph (b)(22)(i)(C) or (E) of this section.

(F) [*Reserved*]

(iv) *Anti-avoidance rules*—(A) *Principal purpose to reduce interest expense*—(*1*) *Treatment as interest expense.* Any expense or loss economically equivalent to interest is treated as interest expense if a principal purpose of structuring the transaction(s) is to reduce an amount incurred by the taxpayer that otherwise would have been described in paragraph (b)(22)(i), (ii), or (iii) of this section. For this purpose, the fact that the taxpayer has a business purpose for obtaining the use of funds does not affect the determination of whether the manner in which the taxpayer structures the transaction(s) is with a principal purpose of reducing the taxpayer's interest expense. In addition, the fact that the taxpayer has obtained funds at a lower pre-tax cost based on the structure of the transaction(s) does not affect the determination of whether the manner in which the taxpayer structures the transaction(s) is with a principal purpose of reducing the taxpayer's interest expense. For purposes of this paragraph (b)(22)(iv)(A)(*1*), any expense or loss is economically equivalent to interest to the extent that the expense or loss is—

(*i*) Deductible by the taxpayer;

(*ii*) Incurred by the taxpayer in a transaction or series of integrated or related transactions in which the taxpayer secures the use of funds for a period of time;

(*iii*) Substantially incurred in consideration of the time value of money; and

(*iv*) Not described in paragraph (b)(22)(i), (ii), or (iii) of this section.

(*2*) *Corresponding treatment of amounts as interest income.* If a taxpayer knows that an expense or loss is treated by the payor as interest expense under paragraph (b)(22)(iv)(A)(*1*) of this section, the taxpayer provides the use of funds for a period of time in the transaction(s) subject to paragraph (b)(22)(iv)(A)(*1*) of this section, the taxpayer earns income or gain with respect to the transaction(s), and such income or gain is substantially earned in consideration of the time value of money provided by the taxpayer, such income or gain is treated as interest income to the extent of the expense or loss treated by the payor as interest expense under paragraph (b)(22)(iv)(A)(*1*) of this section.

(B) *Interest income artificially increased.* Notwithstanding paragraphs (b)(22)(i) through (iii) of this section, any income realized by a taxpayer in a transaction or series of integrated or related transactions is not treated as interest income of the taxpayer if and to the extent that a principal purpose for structuring the transaction(s) is to artificially increase the taxpayer's business interest income. For this purpose, the fact that the taxpayer has a business purpose for holding interest generating assets does not affect the determination of whether the manner in which the taxpayer structures the transaction(s) is with a principal purpose of artificially increasing the taxpayer's business interest income.

(C) *Principal purpose.* Whether a transaction or a series of integrated or related transactions is entered into with a principal purpose described in paragraph (b)(22)(iv)(A) or (B) of this section depends on all the facts and circumstances related to the transaction(s), except for those facts described in paragraph (b)(22)(iv)(A) or (B) of this section. A purpose may be a principal purpose even though it is outweighed by other purposes (taken together or separately). Factors to be taken into account in determining whether one of the taxpayer's principal purposes for entering into the transaction(s) include the taxpayer's normal borrowing rate in the taxpayer's functional currency, whether the taxpayer would enter into the transaction(s) in the ordinary course of the taxpayer's trade or business, whether the parties to the transaction(s) are related persons (within the meaning of section 267(b) or section 707(b)), whether there is a significant and bona fide business purpose for the structure of the transaction(s), whether the transactions are transitory, for example, due to a circular flow of cash or other property, and the substance of the transaction(s).

(D) *Coordination with anti-avoidance rule in § 1.163(j)–2(j).* The anti-avoidance rules in paragraphs (b)(22)(iv)(A) through (C) of this section, rather than the anti-avoidance rules in § 1.163(j)–2(j), apply to determine whether an item is treated as interest expense or interest income.

(v) *Examples.* The examples in this paragraph (b)(22)(v) illustrate the application of paragraph (b)(22)(iv) of this section. Unless otherwise indicated, A, B, C, D, and Bank are domestic C corporations that are publicly traded; the exemption for certain small businesses in § 1.163(j)–2(d) does not apply; A is not engaged in an excepted trade or business; and all amounts of interest expense are deductible except for the potential application of section 163(j).

(A) *Example 1*—(*1*) *Facts.* A is engaged in a manufacturing business and uses the calendar year as its annual accounting period. A's functional currency is the U.S. dollar and A conducts virtually all of its business in the U.S. dollar. A has no connection to Japan or the Japanese yen in the ordinary course of business. A projects that it will have business interest expense of $100x on an existing loan obligation with a stated principal amount of $2,000x (Loan 1) and no business interest income in its taxable year ending December 31, 2021. In early 2021, A enters into the following transactions, which A would not have entered into in the ordinary course of A's trade or business:

(*i*) A enters into a loan obligation in which A borrows Japanese yen from Bank in an amount equivalent to $2,000x with an interest rate of 1 percent (Loan 2) (at the time of the loan, the U.S. dollar equivalent interest rate on a loan of $2,000x is 5 percent);

(*ii*) A enters into a foreign currency swap transaction (FX Swap) with Bank with a notional principal amount of $2,000x under which A receives Japanese yen at 1 percent multiplied by the amount of Japanese yen borrowed from Bank (which for 2021 equals $20x) and pays U.S. dollars at 5 percent multiplied by a notional amount of $2,000x ($100x per year);

(*iii*) The FX Swap is not integrated with Loan 2 under § 1.988–5; and

(*iv*) A enters into a spot transaction with Bank to convert the proceeds of Loan 2 into $2,000x U.S. dollars and A uses the U.S. dollars to repay Loan 1.

(*2*) *Analysis.* A principal purpose of A entering into the transactions with Bank was to try to reduce the amount incurred by A that otherwise would be interest expense; in effect, A sought to alter A's cost of borrowing by converting a substantial portion of its interest expense deductions on Loan 1 into section 165 deductions on the FX Swap ($100x interest expense related to Loan 1 compared to $20x interest expense related to Loan 2 and $80x section 165 deduction). A's functional currency is the U.S. dollar and A conducts virtually all of its business in the U.S. dollar. A has no connection to Japan or the Japanese yen and would not have entered into the transactions in the ordinary course of A's trade or business. The section 165 deductions related to the FX Swap were incurred by A in a series of transactions in which A secured the use of funds for a period of time and were substantially incurred in consideration of the time value of money. As a result, under paragraph (b)(22)(iv)(A)(*1*) of this section, for purposes of section 163(j), the $80x paid by A to Bank on the FX Swap is treated by A as interest expense.

(B) *Example 2*—(*1*) *Facts.* A is engaged in a manufacturing business and uses the calendar year as its annual accounting period. A does not use gold in its manufacturing business. In 2021, A expects to borrow $1,000x for six months. In January 2021, A borrows from B two ounces of gold at a time when the spot price for gold is $500x per ounce. A agrees to return the two ounces of gold in six months. A sells the two ounces of gold to C for $1,000x. A then enters into a contract with D to purchase two ounces of gold six months in the future for $1,013x. In exchange for the use of $1,000x in cash for six months, A has sustained a loss of $13x in connection with these related transactions. A would not have entered into the gold transactions in the ordinary course of A's trade or business.

(*2*) *Analysis.* In a series of related transactions, A has obtained the use of $1,000x for six months and created a loss of $13x substantially incurred in consideration of the time value of money. A would not have entered into the gold transactions in the ordinary course of A's trade or business. A entered into the transactions with a principal purpose of structuring the transactions to reduce its interest expense (in effect, A sought to convert what otherwise would be interest expense into a loss through the transactions). As a result, under paragraph (b)(22)(iv)(A)(*1*) of this section, for purposes of section 163(j), the loss of $13x is treated by A as interest expense.

(C) *Example 3*—(*1*) *Facts.* A is engaged in a manufacturing business and uses the calendar year as its annual accounting period. A's functional currency is the U.S. dollar and A conducts virtually all of its business in the U.S. dollar. A has no connection to Argentina or the Argentine peso as part of its ordinary course of business. As of January 1, 2021, A expects to have adjusted taxable income (as defined in paragraph (b)(1) of this section) of $200x in the taxable year ending December 31, 2021. A also projects that it will have business interest expense of $70x on an existing loan in 2021. A has cash equivalents of $100x on which A expects to earn $5x of business interest income. In early 2021, A enters into the following transactions, which A would not have entered into in the ordinary course of A's trade or business:

(*i*) A enters into a spot transaction with Bank to convert the $100x of cash equivalents into an amount in Argentine pesos equivalent to $100x and A uses the Argentine pesos to purchase an Argentine peso note (Note) issued by a subsidiary of Bank for the Argentine peso equivalent of $100x; the Note pays interest at a 10 percent rate; and

(*ii*) A enters into a foreign currency swap transaction (FX Swap) with Bank with a notional principal amount of $100x under which A pays Argentine pesos at 10 percent multiplied by the amount of Argentine peso principal amount on the Note (which for 2021 equals $10x) and receives U.S. dollars at 5 percent multiplied by a notional amount of $100x ($5x per year).

(*2*) *Analysis.* A principal purpose of A entering into the transactions was to increase the amount of business interest income received by A; in effect, A increased its business interest income by separately accounting for its net deduction of $5x per year on the FX Swap. A's functional currency is the U.S. dollar and A conducts virtually all of its business in the U.S. dollar. A has no connection to Argentina or the Argentine peso and would not have entered into the transactions in the ordinary course of A's trade or business. The FX Swap was incurred by A as a part of a transaction that A entered into with a principal purpose of artificially increasing its business interest income. As a result, under paragraph (b)(22)(iv)(B) of this section, for purposes of section 163(j), the $10x business interest income earned on the Note by A is reduced by $5x (the net $5x paid by A on the FX Swap).

(D) *Example 4*—(*1*) *Facts.* A is wholly owned by FC, a foreign corporation organized in foreign country X. A uses the calendar year for its annual accounting period. FC has a better credit rating than A. A needs to borrow $2,000x in the taxable year ending December 31, 2021, to fund its business operations. A also projects that, if it borrows $2,000x on January 1, 2021, and pays a market rate of interest, it will have business interest expense of $100x in its taxable year ending December 31, 2021. In early 2021, A enters into the following transactions:

(*i*) A enters into a loan obligation in which A borrows $2,000x from Bank with an interest rate of 3 percent (Loan 1);

(*ii*) FC and Bank enter into a guarantee arrangement (Guarantee) under which FC agrees to guarantee Bank that Bank will be timely paid all of the amounts due on Loan 1; and

(*iii*) A enters into a guarantee fee agreement with FC (Guarantee Fee Agreement) under which A agrees to pay FC $40x in return for FC entering into the Guarantee, which was not an agreement that A would have entered into in the ordinary course of A's trade or business.

(*2*) *Analysis.* A principal purpose of A entering into the transactions was to reduce the amount incurred by A that otherwise would be interest expense; in effect, A sought to convert a substantial portion of its interest expense deductions on Loan 1 into section 162 deductions on the Guarantee Fee Agreement ($100x interest expense had A borrowed without the Guarantee compared to $60x interest expense related to Loan 1 and $40x section 162 deduction). A would not have entered into the Guarantee Fee Agreement in the ordinary course of A's trade or business. The $40x section 162 deductions related to the Guarantee Fee Agreement were incurred by A in a series of transactions in which A secured the use of funds for a period of time and were substantially incurred in consideration of the time value of money. As a result, under paragraph (b)(22)(iv)(A)(*1*) of this section, for purposes of section 163(j), the $40x paid by A to FC on the Guarantee Fee Agreement is treated by A as interest expense.

(E) *Example 5*—(*1*) *Facts.* A, B, and C are equal partners in ABC partnership. ABC is considering acquiring an additional loan from a third-party lender to expand its business operations. However, ABC already has significant debt and interest expense. For the purpose of reducing the amount of additional interest expense ABC would have otherwise incurred by borrowing, A agrees to make an additional contribution to ABC for use in its business operations in exchange for a guaranteed payment for the use of capital under section 707(c).

(*2*) *Analysis.* The guaranteed payment is deductible by ABC, incurred by ABC in a transaction in which ABC secures the use of funds for a period of time, substantially incurred in consideration of the time value of money, and not described in paragraph (b)(22)(i), (ii), or (iii) of this section. As a result, the guaranteed payment to A is economically equivalent to the interest that ABC would have incurred on an additional loan from a third-party lender. A principal purpose of A making a contribution in exchange for a guaranteed payment for the use of capital was to reduce the amount incurred by ABC that otherwise would be interest expense. As a result, under paragraph (b)(22)(iv)(A)(*1*) of this section, for purposes of section 163(j), such guaranteed payment is treated as interest expense of ABC for purposes of section 163(j). In addition, under paragraph (b)(22)(iv)(A)(*2*) of this section, if A knows that the guaranteed payment is treated as interest expense of ABC, because A provides the use of funds for a period of time in a transaction subject to paragraph (b)(22)(iv)(A)(*1*) of this section, A earns income or gain with respect to the transaction, and such income or gain is substantially earned in consideration of the time value of money provided by A, the guaranteed payment is treated as interest income of A for purposes of section 163(j).

(23) *Interest expense.* The term *interest expense* means interest that is paid or accrued, or treated as paid or accrued, for the taxable year.

(24) *Interest income.* The term *interest income* means interest that is included in gross income for the taxable year.

(25) *Member.* The term *member* has the meaning provided in § 1.1502–1(b).

(26) *Motor vehicle.* The term *motor vehicle* means a motor vehicle as defined in section 163(j)(9)(C).

(27) *Old section 163(j).* The term *old section 163(j)* means section 163(j) immediately prior to its amendment by Public Law 115–97, 131 Stat. 2054 (2017).

(28) *Ownership change.* The term *ownership change* has the meaning provided in section 382 and the regulations in this part under section 382 of the Code.

(29) *Ownership date.* The term *ownership date* has the meaning provided in section 382 and the regulations in this part under section 382 of the Code.

(30) *Real estate investment trust.* The term *real estate investment trust* (REIT) has the meaning provided in section 856.

(31) *Real property.* The term *real property* includes—

(i) Real property as defined in § 1.469–9(b)(2); and

(ii) Any direct or indirect right, including a license or other contractual right, to share in the appreciation in value of, or the gross or net proceeds or profits generated by, an interest in real property, including net proceeds or profits associated with tolls, rents or other similar fees.

(32) *Regulated investment company.* The term *regulated investment company* (RIC) has the meaning provided in section 851.

(33) *Relevant foreign corporation.* The term *relevant foreign corporation* means any foreign corporation whose classification is relevant under § 301.7701–3(d)(1) for a taxable year, other than solely pursuant to section 881 or 882.

(34) *S corporation.* The term *S corporation* has the meaning provided in section 1361(a)(1).

(35) [*Reserved*]

(36) *Section 163(j) limitation.* The term *section 163(j) limitation* means the limit on the amount of business interest expense that a taxpayer may deduct in a taxable year under section 163(j) and § 1.163(j)–2(b).

(37) *Section 163(j) regulations.* The term *section 163(j) regulations* means this section and §§ 1.163(j)–2 through 1.163(j)–11.

(38) *Separate return limitation year.* The term *separate return limitation year* (SRLY) has the meaning provided in § 1.1502–1(f).

(39) *Separate return year.* The term *separate return year* has the meaning provided in § 1.1502–1(e).

(40) *Separate tentative taxable income.* The term *separate tentative taxable income* with respect to a taxpayer and a taxable year has the meaning provided in § 1.1502–12, but for this purpose computed without regard to the application of the section 163(j) limitation and with the addition of the adjustments made in paragraph (b)(43)(ii) of this section and § 1.163(j)–4(d)(2)(iv).

(41) *Tax-exempt corporation.* The term *tax-exempt corporation* means any tax-exempt organization that is organized as a corporation.

(42) *Tax-exempt organization.* The term *tax-exempt organization* means any entity subject to tax under section 511.

(43) *Tentative taxable income*—(i) *In general.* The term *tentative taxable income,* with respect to a taxpayer and a taxable year, generally is determined in the same manner as taxable income under section 63 but for this purpose computed without regard to the application of the section 163(j) limitation. Tentative taxable income is computed without regard to any disallowed business interest expense carryforwards.

(ii) [Reserved]

(iii) *Special rules for defining tentative taxable income.* (A) For special rules defining the tentative taxable income of a RIC or REIT, see § 1.163(j)–4(b)(4)(ii).

(B) For special rules defining the tentative taxable income of consolidated groups, see § 1.163(j)–4(d)(2)(iv).

(C) For special rules defining the tentative taxable income of a partnership, see § 1.163(j)–6(d)(1).

(D) For special rules defining the tentative taxable income of an S corporation, see § 1.163(j)–6(l)(3).

(E) For special rules clarifying that tentative taxable income takes sections 461(l), 465, and 469 into account, see § 1.163(j)–3(b)(4).

(F) For special rules clarifying that tentative taxable income takes sections 461(l), 465, and 469 into account, see § 1.163(j)–3(b)(4).

(G) For special rules clarifying that tentative taxable income takes sections 461(l), 465, and 469 into account, see § 1.163(j)–3(b)(4).

(44) *Trade or business*—(i) *In general.* The term *trade or business* means a trade or business within the meaning of section 162.

(ii) *Excepted trade or business.* The term *excepted trade or business* means the trade or business of performing services as an employee, an electing real property trade or business, an electing farming business, or an excepted regulated utility trade or business. For additional rules related to excepted trades or businesses, including elections made under section 163(j)(7)(B) and (C), see § 1.163(j)–9.

(iii) *Non-excepted trade or business.* The term *non-excepted trade or business* means any trade or business that is not an excepted trade or business.

(45) *Unadjusted basis.* The term *unadjusted basis* means the basis as determined under section 1012 or other applicable sections of chapter 1 of subtitle A of the Code, including subchapters O (relating to gain or loss on dispositions of property), C (relating to corporate distributions and adjustments), K (relating to partners and partnerships), and P (relating to capital gains and losses) of the Code. Unadjusted basis is determined without regard to any adjustments described in section 1016(a)(2) or (3), any adjustments for tax credits claimed by the taxpayer (for example, under section 50(c)), or any adjustments for any portion of the basis that the taxpayer has elected to treat as an expense (for example, under section 179, 179B, or 179C).

(46) *United States shareholder.* The term *United States shareholder* has the meaning provided in section 951(b).

(c) *Applicability date*—(1) *In general.* Except as provided in paragraphs (c)(2) and (3) of this section, this section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, and before November 13, 2020 so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year. Additionally, taxpayers and their related parties within the meaning of sections 267(b) and 707(b)(1), otherwise relying on the notice of proposed rulemaking that was published on December 28, 2018, in the **Federal Register** (83 FR 67490) in its entirety under § 1.163(j)–1(c), may alternatively choose to follow § 1.163(j)–1(b)(1)(iii), rather than proposed § 1.163(j)–1(b)(1)(iii).

(2) *Anti-avoidance rules.* The anti-avoidance rules in paragraph (b)(22)(iv) of this section apply to transactions entered into on or after September 14, 2020.

(3) *Swaps with significant nonperiodic payments*—(i) *In general.* Except as provided in paragraph (c)(3)(ii) of this section, the rules provided in paragraph (b)(22)(ii) of this section apply to notional principal contracts entered into on or after September 14, 2021. However, taxpayers may choose to apply the rules provided in paragraph (b)(22)(ii) of this section to notional principal contracts entered into before September 14, 2021.

(ii) *Anti-avoidance rule.* The anti-avoidance rules in paragraph (b)(22)(iv) of this section (applied without regard to the references to paragraph (b)(22)(ii) of this section) apply to a notional principal contract entered into on or after September 14, 2020.

§ 1.163(j)–2 Deduction for business interest expense limited.

(a) *Overview.* This section provides general rules regarding the section 163(j) limitation. Paragraph (b) of this section provides rules regarding the basic computation of the section 163(j) limitation. Paragraph (c) of this section provides rules for disallowed business interest expense carryforwards. Paragraph (d) of this section provides rules regarding the small business exemption from the section 163(j) limitation. Paragraph (e) of this section that is part of provides rules regarding real estate mortgage investment conduits (REMICs). Paragraph (f) of this section provides rules regarding the calculation of ATI with respect to certain beneficiaries. Paragraph (g) of this section provides rules regarding tax-exempt organizations. Paragraph (h) of this section provides examples illustrating the application of this section. Paragraph (i) of this section is reserved. Paragraph (j) of this section provides an anti-avoidance rule.

(b) *General rule*—(1) *In general.* Except as otherwise provided in this section or in §§ 1.163(j)–3 through 1.163(j)–11, the amount allowed as a deduction for business interest expense for the taxable year cannot exceed the sum of—

(i) The taxpayer's business interest income for the taxable year;

(ii) 30 percent of the taxpayer's ATI for the taxable year, or zero if the taxpayer's ATI for the taxable year is less than zero; and

(iii) The taxpayer's floor plan financing interest expense for the taxable year.

(2) *50 percent ATI limitation for taxable years beginning in 2019 or 2020*—(i) *In general.* Except as otherwise provided in section 163(j)(10) and paragraph (b)(2) of this section, for any taxable year beginning in 2019 or 2020, paragraph (b)(1)(ii) of this section is applied by substituting 50 percent for 30 percent. The 50 percent ATI limitation does not apply to partnerships for taxable years beginning in 2019. Further, for a partnership taxable year beginning in 2020 for which an election out of section 163(j)(10)(A)(i) has not been made, § 1.163(j)–6(f)(2)(xi) is applied by substituting two for ten-thirds when grossing up each partner's final ATI capacity excess amount.

(ii) *Election out of the 50 percent ATI limitation.* A taxpayer may elect to not have paragraph (b)(2)(i) of this section apply for any taxable year beginning in 2019 or 2020. In the case of a partnership, the election must be made by the partnership and may be made only for taxable years beginning in 2020.

(3) *Election to use 2019 ATI in 2020*—(i) *In general.* Subject to paragraph (b)(3)(ii), a taxpayer may elect to use the taxpayer's ATI for the last taxable year beginning in 2019 (2019 ATI) as the ATI for any taxable year beginning in 2020.

(ii) *Short taxable years.* If an election is made under paragraph (b)(3)(i) of this section for a taxable year beginning in 2020 that is a short taxable year, the ATI for such taxable year is equal to the amount that bears the same ratio to 2019 ATI as the number of months in the short taxable year bears to 12.

(4) *Time and manner of making or revoking the elections.* The rules and procedures regarding the time and manner of making, or revoking, an election under paragraphs (b)(2) and (3) of this section are provided in Revenue Procedure 2020–22, 2020–18 I.R.B. 745, or in other guidance that may be issued (see §§ 601.601(d) and 601.602 of this chapter).

(c) *Disallowed business interest expense carryforward*—(1) *In general.* Any business interest expense disallowed under paragraph (b) of this section, or any disallowed disqualified interest that is properly allocable to a non-excepted trade or business under § 1.163(j)–10, is carried forward to the succeeding taxable year as a disallowed business interest expense carryforward, and is therefore business interest expense that is subject to paragraph (b) of this section in such succeeding taxable year. Disallowed business interest expense carryforwards are not re-allocated between non-excepted and excepted trades or businesses in a succeeding taxable year. Instead, the carryforwards continue to be treated as allocable to a non-excepted trade or business. See § 1.163(j)–10(c)(4).

(2) *Coordination with small business exemption.* If disallowed business interest expense is carried forward under the rules of paragraph (c)(1) of this section to a taxable year in which the small business exemption in paragraph (d) of this section applies to the taxpayer, then the general rule in paragraph (b) of this section does not apply to limit the deduction of the disallowed business interest expense carryforward of the taxpayer in that taxable year. See § 1.163(j)–6(m)(3) for rules applicable to the treatment of excess business interest expense from a partnership that is not subject to section 163(j) in a succeeding taxable year, and see § 1.163(j)–6(m)(4) for rules applicable to S corporations with disallowed business interest expense carryforwards that are not subject to section 163(j) in a succeeding taxable year.

(3) *Cross-references*—(i) For special rules regarding disallowed business interest expense carryforwards for taxpayers that are C corporations, including members of a consolidated group, see § 1.163(j)–5.

(ii) For special rules regarding disallowed business interest expense carryforwards of S corporations, see §§ 1.163(j)–5(b)(2) and 1.163(j)–6(l)(5).

(iii) For special rules regarding disallowed business interest expense carryforwards from partnerships, see § 1.163(j)–6.

(iv)–(v) [Reserved]

(d) *Small business exemption*—(1) *Exemption.* The general rule in paragraph (b) of this section does not apply to any taxpayer, other than a tax shelter as defined in section 448(d)(3), in any taxable year in which the taxpayer meets the gross receipts test of section 448(c) and the regulations in this part under section 448 of the Code for the taxable year. See § 1.163(j)–9(b) for elections available under section 163(j)(7)(B) and 163(j)(7)(C) for real property trades or businesses or farming businesses that also may be exempt small businesses. See § 1.163(j)–6(m) for rules applicable to partnerships and S corporations not subject to section 163(j).

(2) *Application of the gross receipts test*—(i) *In general.* In the case of any taxpayer that is not a corporation or a partnership, and except as provided in paragraphs (d)(2)(ii), (iii), and (iv) of this section, the gross receipts test of section 448(c) and the regulations in this part under section 448 of the Code are applied in the same manner as if such taxpayer were a corporation or partnership.

(ii) *Gross receipts of individuals.* Except as provided in paragraph (d)(2)(iii) of this section (regarding partnership and S corporation interests), an individual taxpayer's gross receipts include all items specified as gross receipts in regulations under section 448(c), whether or not derived in the ordinary course of the taxpayer's trade or business. For purposes of section 163(j), an individual taxpayer's gross receipts do not include inherently personal amounts, including, but not limited to, personal injury awards or settlements with respect to an injury of the individual taxpayer, disability benefits, Social Security benefits received by the taxpayer during the taxable year, and wages received as an employee that are reported on Form W–2.

(iii) *Partners and S corporation shareholders.* Except when the aggregation rules of section 448(c) apply, each partner in a partnership includes a share of partnership gross receipts in proportion to such partner's distributive share (as determined under section 704) of items of gross income that were taken into account by the partnership under section 703. Additionally, each shareholder in an S corporation includes a pro rata share of S corporation gross receipts.

(iv) *Tax-exempt organizations.* For purposes of section 163(j), the gross receipts of a tax-exempt organization include only gross receipts taken into account in determining its unrelated business taxable income.

(e) *REMICs.* For the treatment of interest expense by a REMIC as defined in section 860D, see § 1.860C–2(b)(2)(ii).

(f) *Trusts*—(i) *Calculation of ATI with respect to certain trusts and estates.* The ATI of a trust or a decedent's estate taxable under section 641 is computed without regard to deductions under sections 642(c), 651, and 661.

(ii) *Calculation of ATI with respect to certain beneficiaries.* The ATI of a beneficiary (including a tax-exempt beneficiary) of a trust or a decedent's estate is reduced by any income (including any distributable net income) received from the trust or estate by the beneficiary to the extent such income was necessary to permit a deduction under section 163(j)(1)(B) and § 1.163(j)–2(b) for any business interest expense of the trust or estate that was in excess of any business interest income of the trust or estate.

(g) *Tax-exempt organizations.* Except as provided in paragraph (d) of this section, the section 163(j) limitation applies to tax-exempt organizations for purposes of computing their unrelated business taxable income under section 512. For rules on determining the gross receipts of a tax-exempt organization for purposes of the small business exemption, see paragraph (d)(2)(iv) of this section. For special rules applicable to tax-exempt beneficiaries of a trust or a decedent's estate, see § 1.163(j)–2(f). For special rules applicable to tax-exempt corporations, see § 1.163(j)–4. For special allocation rules applicable to tax-exempt organizations, see § 1.163(j)–10(a)(5).

(h) *Examples.* The examples in this paragraph (h) illustrate the application of section 163(j) and the provisions of this section. Unless otherwise indicated, X and Y are domestic C corporations; C and D are U.S. resident individuals not subject to any foreign income tax; PRS is a domestic partnership with partners who are all individuals; all taxpayers use a calendar taxable year; the exemption for certain small businesses in section 163(j)(3) and paragraph (d) of this section does not apply; and the interest expense would be deductible but for section 163(j).

(1) *Example 1: Limitation on business interest expense deduction*—(i) *Facts.* During its taxable year ending December 31, 2021, X has ATI of $100x. X has business interest expense of $50x, which includes $10x of floor plan financing interest expense, and business interest income of $20x.

(ii) *Analysis.* For the 2021 taxable year, X's section 163(j) limitation is $60x, which is the sum of its business interest income ($20x), plus 30 percent of its ATI ($100x × 30 percent = $30x), plus its floor plan financing interest expense ($10x). See § 1.163(j)–2(b). Because X's business interest expense ($50x) does not exceed X's section 163(j) limitation ($60x), X can deduct all $50x of its business interest expense for the 2021 taxable year.

(2) *Example 2: Carryforward of business interest expense*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (h)(1)(i) of this section, except that X has $80x of business interest expense, which includes $10x of floor plan financing interest expense.

(ii) *Analysis.* As in *Example 1* in paragraph (h)(1)(ii) of this section, X's section 163(j) limitation is $60x. Because X's business interest expense ($80x) exceeds X's section 163(j) limitation ($60x), X may only deduct $60x of its business interest expense for the 2021 taxable year, and the remaining $20x of its business interest expense will be carried forward to the succeeding taxable year as a disallowed business interest expense carryforward. See § 1.163(j)–2(c).

(3) *Example 3: ATI computation*—(i) *Facts.* During the 2020 taxable year, Y has tentative taxable income of $30x, which is determined without regard to the application of the section 163(j) limitation on business interest expense. Y's tentative taxable income includes the following: $20x of business interest income; $50x of business interest expense, which includes $10x of floor plan financing interest expense; $25x of net operating loss deduction under section 172; and $15x of depreciation under section 167, of which $10x is capitalized to inventory under section 263A. Of the $10x capitalized to inventory, only $7x is recovered through cost of goods sold during the 2020 taxable year and $3x remains in ending inventory at the end of the 2020 taxable year. The $3x of ending inventory is recovered through cost of goods sold during the 2021 taxable year. Y also has a disallowed business interest expense carryforward from the prior year of $8x.

(ii) *Analysis.* (A) For purposes of determining the section 163(j) limitation for 2020, Y's disallowed business interest expense carryforward is not taken into account in determining tentative taxable income or ATI. Y's ATI is $90x, calculated as follows:

TABLE 1 TO PARAGRAPH (h)(3)(ii)(A)

Tentative taxable income	$30x
Less:	
Floor plan financing interest	10x
Business interest income	20x
	0x

(B) Plus:

TABLE 2 TO PARAGRAPH (h)(3)(ii)(B)

Business interest expense	$50x
Net operating loss deduction	25x
Depreciation	15x
ATI	90x

(C) For Y's 2021 taxable year, the $3x of ending inventory that is recovered through cost of goods sold in 2021 is not added back to tentative taxable income (TTI) in determining ATI because it was already included as an addback in ATI in Y's 2020 taxable year. See § 1.163(j)–1(b)(1)(iii).

(4) *Example 4: Floor plan financing interest expense*—(i) *Facts.* C is the sole proprietor of an automobile dealership that uses a cash method of accounting. In the 2021 taxable year, C paid $30x of interest on a loan that was obtained to purchase sedans for sale by the dealership. The indebtedness is secured by the sedans purchased with the loan proceeds. In addition, C paid $20x of interest on a loan, secured by the dealership's office equipment, which C obtained to purchase convertibles for sale by the dealership.

(ii) *Analysis.* For the purpose of calculating C's section 163(j) limitation, only the $30x of interest paid on the loan to purchase the sedans is floor plan financing interest expense. The $20x paid on the loan to purchase the convertibles is not floor plan financing interest expense for purposes of section 163(j) because the indebtedness was not secured by the inventory of convertibles. However, because under § 1.163(j)–10 the interest paid on the loan to purchase the convertibles is properly allocable to C's dealership trade or business, and because floor plan financing interest expense is also business interest expense, C has $50x of business interest expense for the 2021 taxable year.

(5) *Example 5: Interest not properly allocable to non-excepted trade or business*—(i) *Facts.* The facts are the same as in *Example 4* in paragraph (h)(4)(i) of this section, except that the $20x of interest C pays is on acquisition indebtedness obtained to purchase C's personal residence and not to purchase convertibles for C's dealership trade or business.

(ii) *Analysis.* Because the $20x of interest expense is not properly allocable to a non-excepted trade or business, and therefore is not business interest expense, C's only business interest expense is the $30x that C pays on the loan used to purchase sedans for sale in C's dealership trade or business. C deducts the $20x of interest related to his residence under the rules of section 163(h), without regard to section 163(j).

(6) *Example 6: Small business exemption*—(i) *Facts.* During the 2021 taxable year, D, the sole proprietor of a trade or business reported on Schedule C, has interest expense properly allocable to that trade or business. D does not conduct an electing real property trade or business or an electing farming business. D also earns gross income from providing services as an employee that is reported on a Form W–2. Under section 448(c) and the regulations in this part under section 448, D has average annual gross receipts of $21 million, including $1 million of wages in each of the three prior taxable years and $2 million of income from investments not related to a trade or business in each of the three prior taxable years. Also, in each of the three prior taxable years, D received $5 million in periodic payments of compensatory damages awarded in a personal injury lawsuit.

(ii) *Analysis.* Section 163(j) does not apply to D for the taxable year, because D qualifies for the small business exemption under § 1.163(j)–2(d). The wages that D receives as an employee and the compensatory damages that D received from D's personal injury lawsuit are not gross receipts, as provided in § 1.163(j)–2(d)(2)(ii). D may deduct all of its business interest expense for the 2021 taxable year without regard to section 163(j).

(7) *Example 7: Partnership with excess business interest expense qualifies for the small business exemption in a succeeding taxable year*—(i) *Facts.* X and Y are equal partners in partnership PRS. In addition to being partners in PRS, X and Y each operate their own sole proprietorships. For the taxable year ending December 31, 2021, PRS is subject to section 163(j) and has excess business interest expense of $10x. For the taxable year ending December 31, 2022, PRS has $40x of business interest expense, and X and Y have $20x of business interest expense from their respective sole proprietorships. For the taxable year ending December 31, 2022, PRS and Y qualify for the small business exemption under § 1.163(j)–2(d), while X is subject to section 163(j) and has a section 163(j) limitation of $22x.

(ii) *Partnership-level analysis.* For the 2021 taxable year, PRS allocates the $10x of excess business interest expense equally to X and Y ($5x each). See § 1.163(j)–6(f)(2). For the 2022 taxable year, section 163(j) does not apply to PRS because PRS qualifies for the small business exemption. As a result, none of PRS's $40x of business interest expense for the 2022 taxable year is subject to the section 163(j) limitation at the partnership level.

(iii) *Partner-level analysis.* For the 2022 taxable year, each partner treats its $5x of excess business interest expense from PRS as paid or accrued in that year. See § 1.163(j)–6(m)(3). This amount becomes business interest expense that each partner must subject to its own section 163(j) limitation, if any. With this $5x, each partner has $25x of business interest expense for the 2022 taxable year ($20x from its sole proprietorship, plus $5x of excess business interest expense treated as paid or accrued in the 2020 taxable year). X deducts $22x of its business interest expense pursuant to its section 163(j) limitation and carries forward the remainder ($3x) as a disallowed business interest expense carryforward to the taxable year ending December 31, 2023. Y is not subject to section 163(j) because Y qualifies for the small business exemption. Y therefore deducts all $25x of its business interest expense for the 2022 taxable year.

(8) *Example 8: Aggregation of gross receipts*—(i) *Facts.* X and Y are domestic C corporations under common control, within the meaning of section 52(a) and § 1.52–1(b). X's only trade or business is a farming business described in § 1.263A–4(a)(4). During the taxable year ending December 31, 2020, X has average annual gross receipts under section 448(c) of $6 million. During the same taxable year, Y has average annual gross receipts under section 448(c) of $21 million.

(ii) *Analysis.* Because X and Y are under common control, they must aggregate gross receipts for purposes of section 448(c) and the small business exemption in § 1.163(j)–2(d). See section 448(c)(2). Therefore, X and Y are both considered to have $27 million in average annual gross receipts for 2020. X and Y must separately apply section 163(j) to determine any limitation on the deduction for business interest expense. Assuming X otherwise meets the requirements in § 1.163(j)–9 in 2020, X may elect for its farming business to be an excepted trade or business.

(i) [Reserved]

(j) *Anti-avoidance rule*—(1) *In general.* Arrangements entered into with a principal purpose of avoiding the rules of section 163(j) or the section 163(j) regulations, including the use of multiple entities to avoid the gross receipts test of section 448(c), may be disregarded or recharacterized by the Commissioner of the IRS to the extent necessary to carry out the purposes of section 163(j).

(2) *Examples.* The examples in this paragraph (j)(2) illustrate the application of this section.

(i) *Example 1*—(A) *Facts.* Individual A operates an excepted trade or business (Business X) and a non-excepted trade or business (Business Y). With a principal purpose of avoiding the rules of section 163(j) or the regulations in this part under section 163(j) of the Code, A contributes Business X to newly-formed C corporation B in exchange for stock; A then causes B to borrow funds from a third party and distributes a portion of the borrowed funds to A for use in Business Y. B takes the position that its interest payments on the debt are not subject to the section 163(j) limitation because B is engaged solely in an excepted trade or business.

(B) *Analysis.* A has entered into an arrangement with a principal purpose of avoiding the rules of section 163(j) or the regulations in this part under section 163(j). Thus, under paragraph (j)(1) of this section, the Commissioner of the IRS may disregard or recharacterize this transaction to the extent necessary to carry out the purposes of section 163(j). In this case, payments of interest on the debt may be recharacterized as payments of interest properly allocable to a non-excepted trade or business subject to the section 163(j) limitation.

(ii) *Example 2*—(A) *Facts.* Partnership UTP has two non-excepted trades or businesses. Business A has gross income of $1000x and gross deductions of $200x. Business B has gross income of $100x and gross deductions of $600x. With a principal purpose of avoiding the rules in section 163(j) or the regulations in this part under section 163(j), UTP and a partner of UTP form partnership LTP and UTP contributes Business B to LTP prior to borrowing funds. UTP takes the position that it does not take its share of LTP gross deductions into account when computing its ATI.

(B) *Analysis.* UTP has entered into an arrangement with a principal purpose of avoiding the rules of section 163(j) or the regulations in this part under section 163(j). Thus, under paragraph (j)(1) of this section, the Commissioner of the IRS may disregard or recharacterize this transaction to the extent necessary to carry out the purposes of section 163(j). In this case, UTP's share of gross deductions from LTP may be recharacterized as gross deductions incurred directly by UTP solely for purposes of computing UTP's ATI.

(k) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

§ 1.163(j)–3 Relationship of the section 163(j) limitation to other provisions affecting interest.

(a) *Overview.* This section contains rules regarding the relationship between section 163(j) and certain other provisions of the Code. Paragraph (b) of this section provides the general rules concerning the relationship between section 163(j) and certain other provisions of the Code. Paragraph (c) of this section provides examples illustrating the application of this section. For rules regarding the relationship between sections 163(j) and 704(d), see § 1.163(j)–6(h)(1) and (2).

(b) *Coordination of section 163(j) with certain other provisions*—(1) *In general.* Section 163(j) and the regulations in this part under section 163(j) of the Code generally apply only to business interest expense that would be deductible in the current taxable year without regard to section 163(j). Thus, for example, a taxpayer must apply § 1.163–8T, if applicable, to determine which items of interest expense are investment interest under section 163(d) before applying the rules in this section to interest expense. Except as otherwise provided in this section, section 163(j) applies after the application of provisions that subject interest expense to disallowance, deferral, capitalization, or other limitation. For the rules that must be applied in determining whether excess business interest is paid or accrued by a partner, see section 163(j)(4)(B)(ii) and § 1.163(j)–6.

(2) *Disallowed interest provisions.* For purposes of section 163(j), business interest expense does not include interest expense that is permanently disallowed as a deduction under another provision of the Code, such as in section 163(e)(5)(A)(i), (f), (l), or (m), or section 264(a), 265, 267A, or 279.

(3) *Deferred interest provisions.* Other than sections 461(l), 465, and 469, Code provisions that defer the deductibility of interest expense, such as section 163(e)(3) and (e)(5)(A)(ii), 267(a)(2) and (3), 1277, or 1282, apply before the application of section 163(j).

(4) *At risk rules, passive activity loss provisions, and limitation on excess business losses of noncorporate taxpayers.* Section 163(j) generally applies to limit the deduction for business interest expense before the application of sections 461(l), 465, and 469. However, in determining tentative taxable income for purposes of computing ATI, sections 461(l), 465, and 469 are taken into account.

(5) *Capitalized interest expenses.* Section 163(j) applies after the application of provisions that require the capitalization of interest, such as sections 263A and 263(g). Capitalized interest expense under those sections is not treated as business interest expense for purposes of section 163(j). For ordering rules that determine whether interest expense is capitalized under section 263A(f), see the regulations under section 263A(f), including § 1.263A–9(g).

(6) *Reductions under section 246A.* Section 246A applies before section 163(j). Any reduction in the dividends received deduction under section 246A reduces the amount of interest expense taken into account under section 163(j).

(7) *Section 381.* Disallowed business interest expense carryforwards are items to which an acquiring corporation succeeds under section 381(a). See section 381(c)(20) and §§ 1.163(j)–5(c) and 1.381(c)(20)–1.

(8) *Section 382.* For rules governing the interaction of sections 163(j) and 382, see section 382(d)(3) and (k)(1), §§ 1.163(j)–5(e) and 1.163(j)–11(c), the regulations in this part under sections 382 and 383 of the Code, and §§ 1.1502–91 through 1.1502–99.

(c) *Examples.* The examples in this paragraph (c) illustrate the application of section 163(j) and the provisions of this section. Unless otherwise indicated, X and Y are calendar-year domestic C corporations; D is a U.S. resident individual not subject to any foreign income tax; none of the taxpayers have floor plan financing interest expense; and the exemption for certain small businesses in § 1.163(j)–2(d) does not apply.

(1) *Example 1: Disallowed interest expense*—(i) *Facts.* In 2021, X has $30x of interest expense. Of X's interest expense, $10x is permanently disallowed under section 265. X's business interest income is $3x and X's ATI is $90x.

(ii) *Analysis.* Under paragraph (b)(2) of this section, the $10x interest expense that is permanently disallowed under section 265 cannot be taken into consideration for purposes of section 163(j) in the 2021 taxable year. X's section 163(j) limitation, or the amount of business interest expense that X may deduct is limited to $30x under § 1.163(j)–2(b), determined by adding X's business interest income ($3x) and 30 percent of X's 2019 ATI ($27x). Therefore, in the 2021 taxable year, none of the $20x of X's deduction for its business interest expense is disallowed under section 163(j).

(2) *Example 2: Deferred interest expense*—(i) *Facts.* In 2021, Y has no business interest income, $120x of ATI, and $70x of interest expense. Of Y's interest expense, $30x is not currently deductible under section 267(a)(2). The $30x expense is allowed as a deduction under section 267(a)(2) in 2022.

(ii) *Analysis.* Under paragraph (b)(3) of this section, section 267(a)(2) is applied before section 163(j). Accordingly, $30x of Y's interest expense cannot be taken into consideration for purposes of section 163(j) in 2021 because it is not currently deductible under section 267(a)(2). Accordingly, in 2021, if the interest expense is properly allocable to a non-excepted trade or business, Y will have $4x of disallowed business interest expense because the $40x of business interest expense in 2021 ($70x − $30x) exceeds 30 percent of its ATI for the taxable year ($36x). The $30x of interest expense not allowed as a deduction in the 2021 taxable year under section 267(a)(2) will be taken into account in determining the business interest expense deduction under section 163(j) in 2022, the taxable year in which it is allowed as a deduction under section 267(a)(2), if it is allocable to a trade or business. Additionally, the $4x of disallowed business interest expense in 2021 will be carried forward to 2022 as a disallowed business interest expense carryforward. See § 1.163(j)–2(c).

(3) *Example 3: Passive activity loss*—(i) *Facts.* D is engaged in a rental activity treated as a passive activity within the meaning of section 469. For the 2021 taxable year, D receives $200x of rental income and incurs $300x of expenses all properly allocable to the rental activity, consisting of $150x of interest expense, $60x of maintenance expenses, and $90x of depreciation expense. D's ATI is $400x.

(ii) *Analysis.* Under paragraph (b)(4) of this section, section 163(j) is applied before the section 469 passive loss rules apply, except that section 469 is taken into account in the determination of tentative taxable income for purposes of computing ATI. D's section 163(j) limitation is $120x, determined by adding to D's business interest income ($0), floor plan financing ($0), and 30 percent of D's ATI ($120x). See § 1.163(j)–2(b). Because D's business interest expense of $150x exceeds D's section 163(j) limitation for 2021, $30x of D's business interest expense is disallowed under section 163(j) and will be carried forward as a disallowed business interest expense carryforward. See § 1.163(j)–2(c). Because the section 163(j) limitation is applied before the limitation under section 469, only $120x of the business interest expense allowable under section 163(j) is included in determining D's passive activity loss limitation for the 2021 tax year under section 469. The $30x of disallowed business interest expense is not an allowable deduction under section 163(j) and, therefore, is not a deduction under section 469 in the current taxable year. See § 1.469–2(d)(8).

(4) *Example 4: Passive activity loss by taxpayer that also participates in a non-passive activity*—(i) *Facts.* For 2021, D has no business interest income and ATI of $1,000x, entirely attributable to a passive activity within the meaning of section 469. D has business interest expense of $1,000x, $900x of which is properly allocable to a passive activity and $100x of which is properly allocable to a non-passive activity in which D materially participates. D has other business deductions that are not subject to section 469 of $600x, and a section 469 passive loss from the previous year of $250x.

(ii) *Analysis.* Under paragraph (b)(4) of this section, section 163(j) is applied before the section 469 passive loss rules apply. D's section 163(j) limitation is $300x, determined by adding D's business interest income ($0), floor plan financing ($0), and 30 percent of D's ATI ($300x)). Next, applying the limitation under section 469 to the $300x business interest expense deduction allowable under section 163(a) and (j), $270x (a proportionate amount of the $300x (0.90 × $300x)) is business interest expense included in determining D's passive activity loss limitation under section 469, and $30x (a proportionate amount of the $300x (0.10 × $300)) is business interest expense not included in determining D's passive activity loss limitation under section 469. Because D's interest expense of $1,000x exceeds 30 percent of its ATI for 2021, $700x of D's interest expense is disallowed under section 163(j) and will be carried forward as a disallowed business interest expense carryforward. Section 469 does not apply to any portion of the $700x disallowed business interest expense because that business interest expense is not an allowable deduction under section 163(j) and, therefore, is not an allowable deduction under section 469 in the current taxable year. See § 1.469–2(d)(8).

(5) *Example 5: ATI calculation with passive activity loss*—(i) *Facts.* D is an individual who engages in a trade or business, V, as a sole proprietorship. D relies on employees to perform most of the work and, as a result, D does not materially participate in V. Therefore, V is a passive activity of D. V is not an excepted trade or business. In Year 1, V generates $500x of passive income, $400x of business interest expense, and $600x of ordinary and necessary expenses deductible under section 162 (not including any interest described in § 1.163(j)–1(b)(22)). No disallowed business interest expense carryforward has been carried to Year 1 from a prior year, and no amounts have been carried over to Year 1 from a prior year under either section 465(a)(2) or section 469(b).

(ii) *Tentative taxable income.* Under § 1.163(j)–1(b)(43), tentative taxable income is determined as though all business interest expense was not subject to the section 163(j) limitation. Sections 461(l), 465, and 469 apply in the determination of tentative taxable income. For year 1, D has $500x of allowable deductions and a $500x tentative passive activity loss under section 469, because D's $1000x of passive expenses exceeds D's $500x of passive income from V. The tentative disallowance of $500x is generally allocated pro rata between D's passive expenses under § 1.469–1T(f)(2)(ii)(A). In this case, fifty percent ($500x of passive activity loss divided by $1000x of total passive expenses) of each category of passive expense is tentatively disallowed: $200x of business interest expense and $300x of section 162 expense. D's tentative taxable income is $0 (zero), which is determined by reducing $500x of gross income by the remaining $200x of business interest expense and $300x of section 162 expense ($500x − $200x − $300x).

(iii) *ATI.* Under section § 1.163(j)–1(b)(1), to determine ATI, D must add business interest expense to tentative taxable income, but only to the extent that the business interest expense reduced tentative taxable income, or $200x. The $200x of business interest expense that was tentatively disallowed under section 469 is not added to tentative taxable income to determine ATI. D's ATI is $200x, which is determined by adding the $200x of business interest expense that reduced tentative taxable income to D's tentative taxable income, or $0 (0 + $200x).

(iv) *Section 163(j) limitation.* D's section 163(j) limitation in Year 1 is D's business interest income, or $0, plus 30 percent of ATI, or $60x (30 percent × $200x ATI), plus D's floor plan financing, or $0, for a total of $60x ($0 + $60x + $0). Before the application of section 469, D has $60x of deductible business interest expense and $340x of disallowed business interest expense carryforward under § 1.163(j)–2(c).

(v) *Passive activity loss.* Because D's passive deductions exceed the passive income from V, and D does not have any passive income from other sources, section 469 applies to limit D's passive loss from V. Having first applied section 163(j), D has $660x of passive expenses, determined by adding D's $60x of business interest expense that is allowed by section 163(j) as a deduction and $600x of section 162 expense ($60x + $600x). D offsets $500x of the passive expenses against $500x of passive income; therefore, D has a passive activity loss of $160x in Year 1, determined as the excess of D's total passive expenses over D's passive income ($660x − $500x). The amount of D's loss from the passive activity that is disallowed under section 469 ($160x) is generally ratably allocated to each of D's passive activity deductions under § 1.469–1T(f)(2)(ii)(A). As a general rule, each deduction is multiplied by the ratio of the total passive loss to total passive expenses (160x/660x). Of D's $60x business interest expense, $14.55x (($160x/$660x) × $60x) is disallowed in Year 1. Additionally, of D's $600x section 162 expense, $145.45x (($160x/$660x) × $600x) is disallowed. The amounts disallowed under section 469(a)(1) and § 1.469–2T(f)(2) are carried over to the succeeding taxable year under section 469(b) and § 1.469–1(f)(4).

(6) *Example 6: Effect of passive activity loss carryforwards*—(i) *Facts.* The facts are the same as in *Example 5* in paragraph (c)(5)(i) of this section. In Year 2, V generates $500x of passive income, $100x of business interest expense, and $0 (zero) of other deductible expenses. D is not engaged in any other trade or business activities. A disallowed business interest expense carryforward of $340x has been carried to Year 2 from Year 1. Under section 469, D has a suspended loss from Year 1 that includes $14.55x of business interest expense and $145.45x of section 162 expense. These amounts are treated as passive activity deductions in Year 2.

(ii) *Tentative taxable income.* To determine D's tentative taxable income, D must first determine D's allowable deductions. In year 2, D has $260x of allowable deductions, which includes $100x of business interest expense generated Year 2, $14.55x of business interest expense disallowed in Year 1 by section 469, and $145.45x of section 162 expense disallowed in Year 1 by section 469 ($100x + $14.55x + $145.45x)). D's disallowed business interest expense carryforward from Year 1 is not taken into account in determining tentative taxable income. See § 1.163(j)–1(b)(43). Additionally, the $14.55x of business interest expense disallowed in Year 1 by section 469 is not business interest expense in Year 2 because it was deductible after the application of section 163(j) (but before the application of section 469) in Year 1. D does not have a tentative passive activity loss in Year 2, because D's $500x of passive income from V exceeds D's $260x of tentative passive expenses. Therefore, D's tentative taxable income in Year 2 is $240x, which is determined by subtracting D's allowable deductions other than disallowed business interest expense carryforwards, or $260x, from D's gross income, or $500x ($500x − $260x).

(iii) *ATI.* D's ATI in Year 2 is $340x, which is determined by adding D's business interest expense, or $100x, to D's tentative taxable income, or $240x ($240x + $100x). Because disallowed business interest expense carryforwards are not taken into account in determining tentative taxable income, there is no corresponding adjustment for disallowed business interest expense carryforwards in calculating ATI. Therefore, there is no adjustment for D's $340x of disallowed business interest expense carryforward in calculating D's ATI. D has no other adjustments to determine ATI.

(iv) *Section 163(j) limitation.* D's section 163(j) limitation in Year 2 is $102x, which is determined by adding D's business interest income, or $0, 30 percent of D's ATI for year 2, $102 ($340x × 30 percent), and D's floor plan financing for Year 2, or $0 ($0 + ($102x) + $0). Accordingly, before the application of section 469 in Year 2, $102x of D's $440x of total business interest expense (determined by adding $340x of disallowed business interest expense carryforward from Year 1 and $100x of business interest expense in Year 2) is deductible. D has $338x of disallowed business interest expense carryforward that will carry forward to subsequent taxable years under § 1.163(j)–2(c), determined by subtracting D's deductible business interest expense in Year 2, or $102x, from D's total business interest expense in Year 2, or $440x ($440x − $102x).

(v) *Section 469.* After applying the section 163(j) limitation, D applies section 469 to determine if any amount of D's expense is a disallowed passive activity loss. For Year 2, D has $262x of passive expenses, determined by adding D's business interest expense deduction allowed by section 163(j) ($102x), D's section 162 expense carried forward from Year 1 under section 469 ($145.45x), and D's interest expense carried forward from Year 1 under section 469 which is not business interest expense in Year 2, or $14.55x ($102x + $145.45x + $14.55x). Therefore, D has $238x of net passive income in Year 2, determined by reducing D's total passive income in Year 2 ($500x), by D's disallowed passive activity loss, or $262x ($500x − $262x). D does not have a passive activity loss in Year 2, and no part of D's $262x of passive expenses is disallowed in Year 2 under section 469.

(7) *Example 7: Capitalized interest expense*—(i) *Facts.* In 2020, X has $50x of interest expense. Of X's interest expense, $10x is required to be capitalized under section 263A. X capitalizes this interest expense to a depreciable asset. X's business interest income is $9x and X's ATI is $80x. X makes the election in § 1.163(j)–2(b)(2)(ii) to use 30 percent, rather than 50 percent, of ATI in determining X's section 163(j) limitation for the 2020 taxable year.

(ii) *Analysis.* Under paragraph (b)(5) of this section, section 263A is applied before section 163(j). Accordingly, $10x of X's interest expense cannot be taken into consideration for purposes of section 163(j) in 2020. Additionally, under paragraph (b)(5) of this section, X's $10 of capitalized interest expense is not business interest expense for purposes of section 163(j). As a result, when X recovers its capitalized interest expense through depreciation deductions, such capitalized interest expense will not be taken into account as business interest expense in determining X's section 163(j) limitation. X's section 163(j) limitation in 2020, or the amount of business interest expense that X may deduct, is limited to $33x under § 1.163(j)–2(b), determined by adding X's business interest income ($9x) and 30 percent of X's 2020 ATI ($24x). X therefore has $7x of disallowed business interest expense in 2020 that will be carried forward to 2021 as a disallowed business interest expense carryforward.

(d) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

§ 1.163(j)–4 General rules applicable to C corporations (including REITs, RICs, and members of consolidated groups) and tax-exempt corporations.

(a) *Scope.* This section provides rules regarding the computation of items of income and expense under section 163(j) for taxpayers that are C corporations, including, for example, members of a consolidated group, REITs, RICs, tax-exempt corporations, and cooperatives. Paragraph (b) of this section provides rules regarding the characterization of items of income, gain, deduction, or loss. Paragraph (c) of this section provides rules regarding adjustments to earnings and profits. Paragraph (d) of this section provides rules applicable to members of a consolidated group. Paragraph (e) of this section provides rules governing the ownership of partnership interests by members of a consolidated group. Paragraph (f) of this section provides cross-references to other rules within the 163(j) regulations that may be applicable to C corporations.

(b) *Characterization of items of income, gain, deduction, or loss*—(1) *Interest expense and interest income.* Solely for purposes of section 163(j), all interest expense of a taxpayer that is a C corporation is treated as properly allocable to a trade or business. Similarly, solely for purposes of section 163(j), all interest income of a taxpayer that is a C corporation is treated as properly allocable to a trade or business. For rules governing the allocation of interest expense and interest income between excepted and non-excepted trades or businesses, see § 1.163(j)–10.

(2) *Adjusted taxable income.* Solely for purposes of section 163(j), all items of income, gain, deduction, or loss of a taxpayer that is a C corporation are treated as properly allocable to a trade or business. For rules governing the allocation of tax items between excepted and non-excepted trades or businesses, see § 1.163(j)–10.

(3) *Investment interest, investment income, investment expenses, and certain other tax items of a partnership with a C corporation partner*—(i) *Characterization as expense or income properly allocable to a trade or business.* For purposes of section 163(j), any investment interest, investment income, or investment expense (within the meaning of section 163(d)) that a partnership pays, receives, or accrues and that is allocated to a C corporation partner as a separately stated item is treated by the C corporation partner as properly allocable to a trade or business of that partner. Similarly, for purposes of section 163(j), any other tax items of a partnership that are neither properly allocable to a trade or business of the partnership nor described in section 163(d) and that are allocated to a C corporation partner as separately stated items are treated as properly allocable to a trade or business of that partner.

(ii) *Effect of characterization on partnership.* The characterization of a partner's tax items pursuant to paragraph (b)(3)(i) of this section does not affect the characterization of these items at the partnership level.

(iii) *Separately stated interest expense and interest income of a partnership not treated as excess business interest expense or excess taxable income of a C corporation partner.* Investment interest expense and other interest expense of a partnership that is treated as business interest expense by a C corporation partner under paragraph (b)(3)(i) of this section is not treated as excess business interest expense of the partnership. Investment interest income and other interest income of a partnership that is treated as business interest income by a C corporation partner under paragraph (b)(3)(i) of this section is not treated as excess taxable income of the partnership. For rules governing excess business interest expense and excess taxable income, see § 1.163(j)–6.

(iv) *Treatment of deemed inclusions of a domestic partnership that are not allocable to any trade or business.* If a United States shareholder that is a domestic partnership includes amounts in gross income under sections 951(a) or 951A(a) that are not properly allocable to a trade or business of the domestic partnership, then, notwithstanding paragraph (b)(3)(i) of this section, to the extent a C corporation partner, including an indirect partner in the case of tiered partnerships, takes such amounts into account as a distributive share in accordance with section 702 and § 1.702–1(a)(8)(ii), the C corporation partner may not treat such amounts as properly allocable to a trade or business of the C corporation partner.

(4) *Application to RICs and REITs*—(i) *In general.* Except as otherwise provided in paragraphs (b)(4)(ii) and (iii) of this section, the rules in this paragraph (b) apply to RICs and REITs.

(ii) *Tentative taxable income of RICs and REITs.* The tentative taxable income of a RIC or REIT for purposes of calculating ATI is the tentative taxable income of the corporation, without any adjustment that would be made under section 852(b)(2) or 857(b)(2) to compute investment company taxable income or real estate investment trust taxable income, respectively. For example, the tentative taxable income of a RIC or REIT is not reduced by the deduction for dividends paid, but is reduced by the dividends received deduction (DRD) and the other deductions described in sections 852(b)(2)(C) and 857(b)(2)(A). See paragraph (b)(4)(iii) of this section for an adjustment to ATI in respect of these items.

(iii) *Other adjustments to adjusted taxable income for RICs and REITs.* In the case of a taxpayer that, for a taxable year, is a RIC to which section 852(b) applies or a REIT to which section 857(b) applies, the taxpayer's ATI for the taxable year is increased by the amounts of any deductions described in section 852(b)(2)(C) or 857(b)(2)(A).

(5) *Application to tax-exempt corporations.* The rules in this paragraph (b) apply to a tax-exempt corporation only with respect to that corporation's items of income, gain, deduction, or loss that are taken into account in computing the corporation's unrelated business taxable income, as defined in section 512.

(6) *Adjusted taxable income of cooperatives.* Solely for purposes of computing the ATI of a cooperative under § 1.163(j)–1(b)(1), tentative taxable income is not reduced by the amount of any patronage dividend under section 1382(b)(1) or by any amount paid in redemption of nonqualified written notices of allocation distributed as patronage dividends under section 1382(b)(2) (for cooperatives subject to taxation under sections 1381 through 1388), any amount described in section 1382(c) (for

cooperatives described in section 1381(a)(1) and section 521), or any equivalent amount deducted by an organization that operates on a cooperative basis but is not subject to taxation under sections 1381 through 1388.

(7) *Examples.* The principles of this paragraph (b) are illustrated by the following examples. For purposes of the examples in this paragraph (b)(7) of this section, T is a taxable domestic C corporation whose taxable year ends on December 31; T is neither a consolidated group member nor a RIC or a REIT; neither T nor PS1, a domestic partnership, owns at least 80 percent of the stock of any corporation; neither T nor PS1 qualifies for the small business exemption in § 1.163(j)–2(d) or is engaged in an excepted trade or business; T has no floor plan financing expense; all interest expense is deductible except for the potential application of section 163(j); and the facts set forth the only corporate or partnership activity.

(i) *Example 1: C corporation items properly allocable to a trade or business*—(A) *Facts.* In taxable year 2021, T's tentative taxable income (without regard to the application of section 163(j)) is $320x. This amount is comprised of the following tax items: $1,000x of revenue from inventory sales; $500x of ordinary and necessary business expenses (excluding interest and depreciation); $200x of interest expense; $50x of interest income; $50x of depreciation deductions under section 168; and a $20x gain on the sale of stock.

(B) *Analysis.* For purposes of section 163(j), each of T's tax items is treated as properly allocable to a trade or business. Thus, T's ATI for the 2021 taxable year is $520x ($320x of tentative taxable income + $200x business interest expense − $50x business interest income + $50x depreciation deductions = $520x), and its section 163(j) limitation for the 2021 taxable year is $206x ($50x of business interest income + 30 percent of its ATI (30 percent × $520x) = $206x). As a result, all $200x of T's interest expense is deductible in the 2021 taxable year under section 163(j).

(C) *Taxable year beginning in 2022.* The facts are the same as in *Example 1* in paragraph (b)(7)(i)(A) of this section, except that the taxable year begins in 2022 and therefore depreciation deductions are not added back to ATI under § 1.163(j)–1(b)(1)(i)(E). As a result, T's ATI for 2022 is $470x ($320x of tentative taxable income + $200x business interest expense − $50x business interest income = $470x), and its section 163(j) limitation for the 2022 taxable year is $191x ($50x of business interest income + 30 percent of its ATI (30 percent × $470x) = $191x). As a result, T may only deduct $191x of its business interest expense for the taxable year, and the remaining $9x is carried forward to the 2023 taxable year as a disallowed business interest expense carryforward. See § 1.163(j)–2(c).

(ii) *Example 2: C corporation partner*—(A) *Facts.* T and individual A each own a 50 percent interest in PS1, a general partnership. PS1 borrows funds from a third party (Loan 1) and uses those funds to buy stock in publicly-traded corporation X. PS1's only activities are holding X stock (and receiving dividends) and making payments on Loan 1. In the 2021 taxable year, PS1 receives $150x in dividends and pays $100x in interest on Loan 1.

(B) *Analysis.* For purposes of section 163(d) and (j), PS1 has investment interest expense of $100x and investment income of $150x, and PS1 has no interest expense or interest income that is properly allocable to a trade or business. PS1 allocates its investment interest expense and investment income equally to its two partners pursuant to § 1.163(j)–6(k). Pursuant to paragraph (b)(3) of this section, T's allocable share of PS1's investment interest expense is treated as a business interest expense of T, and T's allocable share of PS1's investment income is treated as properly allocable to a trade or business of T. This business interest expense is not treated as excess business interest expense, and this income is not treated as excess taxable income. See paragraph (b)(3)(iii) of this section. T's treatment of its allocable share of PS1's investment interest expense and investment income as business interest expense and income properly allocable to a trade or business, respectively, does not affect the character of these items at the PS1 level and does not affect the character of A's allocable share of PS1's investment interest and investment income.

(C) *Partnership engaged in a trade or business.* The facts are the same as in *Example 2* in paragraph (b)(7)(ii)(A) of this section, except that PS1 also is engaged in Business 1, and PS1 borrows funds from a third party to finance Business 1 (Loan 2). In 2021, Business 1 earns $150x of net income (excluding interest expense and depreciation), and PS1 pays $100x of interest on Loan 2. For purposes of section 163(d) and (j), PS1 treats the interest paid on Loan 2 as properly allocable to a trade or business. As a result, PS1 has investment interest expense of $100x (attributable to Loan 1), business interest expense of $100x (attributable to Loan 2), $150x of investment income, and $150x of income from Business 1. PS1's ATI is $150x (its net income from Business 1 excluding interest and depreciation), and its section 163(j) limitation is $45x (30 percent × $150x). Pursuant to § 1.163(j)–6, PS1 has $55x of excess business interest expense ($100x − $45x), half of which ($27.5x) is allocable to T. Additionally, pursuant to paragraph (b)(3)(i) of this section, T's allocable share of PS1's investment interest expense ($50x) is treated as a business interest expense of T for purposes of section 163(j), and T's allocable share of PS1's investment income ($75x) is treated as properly allocable to a trade or business of T. Therefore, with respect to T's interest in PS1, T is treated as having $50x of business interest expense that is not treated as excess business interest expense, $75x of income that is properly allocable to a trade or business, and $27.5x of excess business interest expense.

(c) *Effect on earnings and profits*—(1) *In general.* In the case of a taxpayer that is a domestic C corporation, except as otherwise provided in paragraph (c)(2) of this section, the disallowance and carryforward under § 1.163(j)–2 (and § 1.163(j)–5, in the case of a taxpayer that is a consolidated group member) of a deduction for business interest expense of the taxpayer or of a partnership in which the taxpayer is a partner does not affect whether or when the business interest expense reduces the taxpayer's earnings and profits. In the case of a foreign corporation, the disallowance and carryforward of a deduction for the corporation's business interest expense under § 1.163(j)–2 does not affect whether and when such business interest expense reduces the corporation's earnings and profits. Thus, for example, if a United States person has elected under section 1295 to treat a passive foreign investment company (as defined in section 1297) (PFIC) as a qualified electing fund, then the disallowance and carryforward of a deduction for the PFIC's business interest expense under § 1.163(j)–2 does not affect whether or when such business interest expense reduces the PFIC's earnings and profits.

(2) *Special rule for RICs and REITs.* In the case of a taxpayer that is a RIC or a REIT for the taxable year in which a deduction for the taxpayer's business interest expense is disallowed under § 1.163(j)–2(b), or in which the RIC or REIT is allocated any excess business interest expense from a partnership under section 163(j)(4)(B)(i) and § 1.163(j)–6, the taxpayer's earnings and profits are adjusted in the taxable year

or years in which the business interest expense is deductible or, if earlier, in the first taxable year for which the taxpayer no longer is a RIC or a REIT.

(3) *Special rule for partners that are C corporations.* If a taxpayer that is a C corporation is allocated any excess business interest expense from a partnership, and if all or a portion of the excess business interest expense has not yet been treated as business interest expense by the taxpayer at the time of the taxpayer's disposition of all or a portion of its interest in the partnership, the taxpayer must increase its earnings and profits immediately prior to the disposition by an amount equal to the amount of the basis adjustment required under section 163(j)(4)(B)(iii)(II) and § 1.163(j)–6(h)(3).

(4) *Examples.* The principles of this paragraph (c) are illustrated by the following examples. For purposes of the examples in this paragraph (c)(4), except as otherwise provided in the examples, X is a taxable domestic C corporation whose taxable year ends on December 31; X is not a member of a consolidated group; X does not qualify for the small business exemption under § 1.163(j)–2(d); X is not engaged in an excepted trade or business; X has no floor plan financing indebtedness; all interest expense is deductible except for the potential application of section 163(j); X has no accumulated earnings and profits at the beginning of the 2021 taxable year; and the facts set forth the only corporate activity.

(i) *Example 1: Earnings and profits of a taxable domestic C corporation other than a RIC or a REIT*—(A) *Facts.* X is a corporation that does not intend to qualify as a RIC or a REIT for its 2021 taxable year. In that year, X has tentative taxable income (without regard to the application of section 163(j)) of $0, which includes $100x of gross income and $100x of interest expense on a loan from an unrelated third party. X also makes a $100x distribution to its shareholders that year.

(B) *Analysis.* The $100x of interest expense is business interest expense for purposes of section 163(j) (see paragraph (b)(1) of this section). X's ATI in the 2021 taxable year is $100x ($0 of tentative taxable income computed without regard to $100x of business interest expense). Thus, X may deduct $30x of its $100x of business interest expense in the 2021 taxable year under § 1.163(j)–2(b) (30 percent × $100x), and X may carry forward the remainder ($70x) to X's 2022 taxable year as a disallowed business interest expense carryforward under § 1.163(j)–2(c). Although X may not currently deduct all $100x of its business interest expense in the 2021 taxable year, X must reduce its earnings and profits in that taxable year by the full amount of its business interest expense ($100x) in that taxable year. As a result, no portion of X's distribution of $100x to its shareholders in the 2021 taxable year is a dividend within the meaning of section 316(a).

(ii) *Example 2: RIC adjusted taxable income and earnings and profits*—(A) *Facts.* X is a corporation that intends to qualify as a RIC for its 2021 taxable year. In that taxable year, X's only items are $100x of interest income, $50x of dividend income from C corporations that only issue common stock and in which X has less than a twenty percent interest (by vote and value), $10x of net capital gain, and $125x of interest expense. None of the dividends are received on debt financed portfolio stock under section 246A. The DRD determined under section 243(a) with respect to X's $50x of dividend income is $25x. X pays $42x in dividends to its shareholders, meeting the requirements of section 562 during X's 2021 taxable year, including $10x that X reports as capital gain dividends in written statements furnished to X's shareholders.

(B) *Analysis.* (*1*) Under paragraph (b) of this section, all of X's interest expense is considered business interest expense, all of X's interest income is considered business interest income, and all of X's other income is considered to be properly allocable to a trade or business. Under paragraph (b)(4)(ii) of this section, prior to the application of section 163(j), X's tentative taxable income is $10x ($100x business interest income + $50x dividend income + $10x net capital gain − $125x business interest expense − $25x DRD = $10x). Under paragraph (b)(4)(iii) of this section, X's ATI is increased by the DRD. As such, X's ATI for the 2021 taxable year is $60x ($10x tentative taxable income + $125x business interest expense − $100x business interest income + $25x DRD = $60x).

(*2*) X may deduct $118x of its $125x of business interest expense in the 2021 taxable year under section 163(j)(1) ($100x business interest income + (30 percent × $60x of ATI) = $118x), and X may carry forward the remainder ($7x) to X's 2022 taxable year. See § 1.163(j)–2(b) and (c).

(*3*) After the application of section 163(j), X has taxable income of $17x ($100x interest income + $50x dividend income + $10x capital gain − $25x DRD − $118x allowable interest expense = $17x) for the 2021 taxable year. X will have investment company taxable income (ICTI) in the amount of $0 ($17x taxable income − $10x capital gain + $25x DRD − $32x dividends paid deduction for ordinary dividends = $0). The excess of X's net capital gain ($10x) over X's dividends paid deduction determined with reference to capital gain dividends ($10x) is also $0.

(*4*) Under paragraph (c)(2) of this section, X will not reduce its earnings and profits by the amount of interest expense disallowed as a deduction in the 2021 taxable year under section 163(j). Thus, X has current earnings and profits in the amount of $42x ($100x interest income + $50x dividend income + $10x capital gain − $118x allowable business interest expense = $42x) before giving effect to dividends paid during the 2021 taxable year.

(iii) *Example 3: Carryforward of disallowed interest expense*—(A) *Facts.* The facts are the same as the facts in *Example 2* in paragraph (c)(4)(ii)(A) of this section for the 2021 taxable year. In addition, X has $50x of interest income and $20x of interest expense for the 2022 taxable year.

(B) *Analysis.* Under paragraph (b) of this section, all of X's interest expense is considered business interest expense, all of X's interest income is considered business interest income, and all of X's other income is considered to be properly allocable to a trade or business. Because X's $50x of business interest income exceeds the $20x of business interest expense from the 2022 taxable year and the $7x of disallowed business interest expense carryforward from the 2021 taxable year, X may deduct $27x of business interest expense in the 2022 taxable year. Under paragraph (c)(2) of this section, X must reduce its current earnings and profits for the 2022 taxable year by the full amount of the deductible business interest expense ($27x).

(iv) *Example 4: REIT adjusted taxable income and earnings and profits*—(A) *Facts.* X is a corporation that intends to qualify as a REIT for its 2021 taxable year. X is not engaged in an excepted trade or business and is not engaged in a trade or business that is eligible to make any election under section 163(j)(7). In that year, X's only items are $100x of mortgage interest income, $30x of dividend income from C corporations that only issue common stock and in which X has less than a ten percent interest (by vote and value), $10x of net capital gain from the sale of mortgages on real property that is not property described in section 1221(a)(1), and $125x of interest expense. None of the dividends are received on debt financed portfolio stock under section 246A. The DRD determined under section 243(a) with respect to X's $30x of dividend income is $15x. X pays $28x in dividends meeting the requirements of section 562 during X's 2021 taxable year, including $10x that X properly designates as capital gain dividends under section 857(b)(3)(B).

(B) *Analysis.* (*1*) Under paragraph (b) of this section, all of X's interest expense is considered business interest expense, all of X's interest income is considered business interest income, and all of X's other income is considered to be properly allocable to a trade or business. Under paragraph (b)(4)(ii) of this section, prior to the application of section 163(j), X's tentative taxable income is $0 ($100x business interest income + $30x dividend income + $10x net capital gain − $125x business interest expense − $15x DRD = $0). Under paragraph (b)(4)(iii) of this section, X's ATI is increased by the DRD. As such, X's ATI for the 2021 taxable year is $40x ($0 tentative taxable income + $125x business interest expense − $100x business interest income + $15x DRD = $40x).

(*2*) X may deduct $112x of its $125x of business interest expense in the 2021 taxable year under section 163(j)(1) ($100x business interest income + (30 percent × $40x of ATI) = $112x), and X may carry forward the remainder of its business interest expense ($13x) to X's 2022 taxable year.

(*3*) After the application of section 163(j), X has taxable income of $13x ($100x business interest income + $30x dividend income + $10x capital gain − $15x DRD − $112x allowable business interest expense = $13x) for the 2021 taxable year. X will have real estate investment trust taxable income (REITTI) in the amount of $0 ($13x taxable income + $15x of DRD − $28x dividends paid deduction = $0).

(*4*) Under paragraph (c)(2) of this section, X will not reduce earnings and profits by the amount of business interest expense disallowed as a deduction in the 2021 taxable year. Thus, X has current earnings and profits in the amount of $28x ($100x business interest income + $30x dividend income + $10x capital gain − $112x allowable business interest expense = $28x) before giving effect to dividends paid during X's 2021 taxable year.

(v) *Example 5: Carryforward of disallowed interest expense*—(A) *Facts.* The facts are the same as in *Example 4* in paragraph (c)(4)(iv)(A) of this section for the 2021 taxable year. In addition, X has $50x of mortgage interest income and $20x of interest expense for the 2022 taxable year. X has no other tax items for the 2022 taxable year.

(B) *Analysis.* Because X's $50x of business interest income exceeds the $20x of business interest expense from the 2022 taxable year and the $13x of disallowed business interest expense carryforwards from the 2021 taxable year, X may deduct $33x of business interest expense in 2022. Under paragraph (c)(2) of this section, X must reduce its current earnings and profits for 2022 by the full amount of the deductible interest expense ($33x).

(d) *Special rules for consolidated groups*—(1) *Scope.* This paragraph (d) provides rules applicable to members of a consolidated group. For all members of a consolidated group for a consolidated return year, the computations required by section 163(j) and the regulations in this part under section 163(j) are made in accordance with the rules of this paragraph (d) unless otherwise provided elsewhere in the section 163(j) regulations. For rules governing the ownership of partnership interests by members of a consolidated group, see paragraph (e) of this section.

(2) *Calculation of the section 163(j) limitation for members of a consolidated group*—(i) *In general.* A consolidated group has a single section 163(j) limitation, the absorption of which is governed by § 1.163(j)–5(b)(3)(ii).

(ii) *Interest.* For purposes of determining whether amounts, other than amounts in respect of intercompany obligations (as defined in § 1.1502–13(g)(2)(ii)), intercompany items (as defined in § 1.1502–13(b)(2)), or corresponding items (as defined in § 1.1502–13(b)(3)), are treated as interest within the meaning of § 1.163(j)–1(b)(22), all members of a consolidated group are treated as a single taxpayer.

(iii) *Calculation of business interest expense and business interest income for a consolidated group.* For purposes of calculating the section 163(j) limitation for a consolidated group, the consolidated group's current-year business interest expense and business interest income, respectively, are the sum of each member's current-year business interest expense and business interest income, including amounts treated as business interest expense and business interest income under paragraph (b)(3) of this section.

(iv) *Calculation of adjusted taxable income.* For purposes of calculating the ATI for a consolidated group, the tentative taxable income is the consolidated group's consolidated taxable income, determined under § 1.1502–11 but without regard to any carryforwards or disallowances under section 163(j). Further, for purposes of calculating the ATI of the group, intercompany items and corresponding items are disregarded to the extent that they offset in amount. Thus, for example, certain portions of the intercompany items and corresponding items of a group member engaged in a non-excepted trade or business will not be included in ATI to the extent that the counterparties to the relevant intercompany transactions are engaged in one or more excepted trades or businesses.

(v) *Treatment of intercompany obligations*—(A) *In general.* Except as otherwise provided in paragraph (d)(2)(v)(B) of this section, for purposes of determining a member's business interest expense and business interest income, and for purposes of calculating the consolidated group's ATI, all intercompany obligations, as defined in § 1.1502–13(g)(2)(ii), are disregarded. Therefore, except as otherwise provided in paragraph (d)(2)(v)(B) of this section, interest expense and interest income from intercompany obligations are not treated as business interest expense and business interest income.

(B) *Repurchase premium.* This paragraph (d)(2)(v)(B) applies if a member of a consolidated group purchases an obligation of another member of the same consolidated group in a transaction to which § 1.1502–13(g)(5) applies. Notwithstanding the general rule of paragraph (d)(2)(v)(A) of this section, if, as a result of the deemed satisfaction of the obligation under § 1.1502–13(g)(5)(ii), the debtor member has repurchase premium that is deductible under § 1.163–7(c), such repurchase premium is treated as interest that is subject to the section 163(j) limitation. See § 1.163(j)–1(b)(22)(i)(H).

(3) *Investment adjustments.* For rules governing investment adjustments within a consolidated group, see § 1.1502–32(b).

(4) *Examples.* The principles in this paragraph (d) are illustrated by the following examples. For purposes of the examples in this paragraph (d)(4), S is a member of the calendar-year consolidated group of which P is the common parent; the P group does not qualify for the small business exemption in § 1.163(j)–2(d); no member of the P group is engaged in an excepted trade or business; all interest expense is deductible except for the potential application of section 163(j); and the facts set forth the only corporate activity.

(i) *Example 1: Calculation of the section 163(j) limitation*—(A) *Facts.* In the 2021 taxable year, P has $50x of separate tentative taxable income after taking into account $65x of interest paid on a loan from a third party (without regard to any disallowance under section 163(j)) and $35x of depreciation deductions under section 168. In turn, S has $40x of separate tentative taxable income in the 2021 taxable year after taking into account $10x of depreciation deductions under section 168. S has no interest expense in the 2021 taxable year. The P group's tentative taxable income the 2021 taxable year is $90x, determined under § 1.1502–11 without regard to any disallowance under section 163(j).

(B) *Analysis.* As provided in paragraph (b)(1) of this section, P's interest expense is treated as business interest expense for purposes of section 163(j). If P and S were to apply the section 163(j) limitation on a separate-entity basis, then P's ATI would be $150x ($50x + $65x + $35x = $150x), its section 163(j) limitation would be $45x (30 percent × $150x = $45x), and a deduction for $20x of its $65x of business interest expense would be disallowed in the 2021 taxable year under section 163(j). However, as provided in paragraph (d)(2) of this section, the P group computes a single section 163(j) limitation, and that computation begins with the P group's tentative taxable income (as determined prior to the application of section 163(j)), or $90x. The P group's ATI is $200x ($50x + $40x + $65x + $35x + $10x = $200x). Thus, the P group's section 163(j) limitation for the 2021 taxable year is $60x (30 percent × $200x = $60x). As a result, all but $5x of the P group's business interest expense is deductible in the 2021 taxable year. P carries over the $5x of disallowed business interest expense to the succeeding taxable year.

(ii) *Example 2: Intercompany obligations*—(A) *Facts.* On January 1, 2021, G, a corporation unrelated to P and S, lends P $100x in exchange for a note that accrues interest at a 10 percent annual rate. A month later, P lends $100x to S in exchange for a note that accrues interest at a 12 percent annual rate. In 2021, P accrues and pays $10x of interest to G on P's note, and S accrues and pays $12x of interest to P on S's note. For that year, the P group's only other items of income, gain, deduction, and loss are $40x of income earned by S from the sale of inventory, and a $30x deductible expense arising from P's payment of tort liability claims.

(B) *Analysis.* As provided in paragraph (d)(2)(v) of this section, the intercompany obligation between P and S is disregarded in determining P and S's business interest expense and business interest income and in determining the P group's ATI. For purposes of section 163(j), P has $10x of business interest expense and a $30x deduction for the payment of tort liability claims, and S has $40x of income. The P group's ATI is $10x ($40x − $30x = $10x), and its section 163(j) limitation is $3x (30 percent × $10x = $3x). The P group may deduct $3x of its business interest expense in the 2021 taxable year. A deduction for P's remaining $7x of business interest expense is disallowed in the 2021 taxable year, and this amount is carried forward to the 2022 taxable year.

(e) *Ownership of partnership interests by members of a consolidated group.*

(1) [Reserved]

(2) *Change in status of a member.* A change in status of a member (that is, becoming or ceasing to be a member of the group) is not treated as a disposition for purposes of section 163(j)(4)(B)(iii)(II) and § 1.163(j)–6(h)(3).

(3) *Basis adjustments under § 1.1502–32.* A member's allocation of excess business interest expense from a partnership and the resulting decrease in basis in the partnership interest under section 163(j)(4)(B)(iii)(I) is not a noncapital, nondeductible expense for purposes of § 1.1502–32(b)(3)(iii). Additionally, an increase in a member's basis in a partnership interest under section 163(j)(4)(B)(iii)(II) to reflect excess business interest expense not deducted by the consolidated group is not tax-exempt income for purposes of § 1.1502–32(b)(3)(ii). Investment adjustments are made under § 1.1502–32(b)(3)(i) when the excess business interest expense from the partnership is converted into business interest expense, deducted, and absorbed by the consolidated group. See § 1.1502–32(b).

(4) *Excess business interest expense and § 1.1502–36.* Excess business interest expense is a Category D asset within the meaning of § 1.1502–36(d)(4)(i).

(f) *Cross-references.* For rules governing the treatment of disallowed business interest expense carryforwards for C corporations, including rules governing the treatment of disallowed business interest expense carryforwards when members enter or leave a consolidated group, see § 1.163(j)–5. For rules governing the application of section 163(j) to a C corporation or a consolidated group engaged in both excepted and non-excepted trades or businesses, see § 1.163(j)–10.

(g) *Applicability date*—(1) *In general.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

(2) [Reserved]

§ 1.163(j)–5 General rules governing disallowed business interest expense carryforwards for C corporations.

(a) *Scope and definitions*—(1) *Scope.* This section provides rules regarding disallowed business interest expense carryforwards for taxpayers that are C corporations, including members of a consolidated group. Paragraph (b) of this section provides rules regarding the treatment of disallowed business interest expense carryforwards. Paragraph (c) of this section provides a cross-reference to other rules regarding disallowed business interest expense carryforwards in transactions to which section 381(a) applies. Paragraph (d) of this section provides rules regarding limitations on disallowed business interest expense carryforwards from separate return limitation years (SRLYs). Paragraph (e) of this section provides cross-references to other rules regarding the application of section 382 to disallowed business interest expense carryforwards. Paragraph (f) of this section provides a cross-reference to other rules regarding the overlap of the SRLY limitation with section 382. Paragraph (g) of this section references additional rules that may limit the deductibility of interest or the use of disallowed business interest expense carryforwards.

(2) *Definitions*—(i) *Allocable share of the consolidated group's remaining section 163(j) limitation.* The term *allocable share of the consolidated group's remaining section 163(j) limitation* means, with respect to any member of a consolidated group, the product of the consolidated group's remaining section 163(j) limitation and the member's remaining current-year interest ratio.

(ii) *Consolidated group's remaining section 163(j) limitation.* The term *consolidated group's remaining section 163(j) limitation* means the amount of the consolidated group's section 163(j) limitation calculated pursuant to

§ 1.163(j)–4(d)(2), reduced by the amount of interest deducted by members of the consolidated group pursuant to paragraph (b)(3)(ii)(C)(*2*) of this section.

(iii) *Remaining current-year interest ratio.* The term *remaining current-year interest ratio* means, with respect to any member of a consolidated group for a particular taxable year, the ratio of the remaining current-year business interest expense of the member after applying the rule in paragraph (b)(3)(ii)(C)(*2*) of this section, to the sum of the amounts of remaining current-year business interest expense for all members of the consolidated group after applying the rule in paragraph (b)(3)(ii)(C)(*2*) of this section.

(b) *Treatment of disallowed business interest expense carryforwards*—(1) *In general.* The amount of any business interest expense of a C corporation not allowed as a deduction for any taxable year as a result of the section 163(j) limitation is carried forward to the succeeding taxable year as a disallowed business interest expense carryforward under section 163(j)(2) and § 1.163(j)–2(c).

(2) *Deduction of business interest expense.* For a taxpayer that is a C corporation, current-year business interest expense is deducted in the current taxable year before any disallowed business interest expense carryforwards from a prior taxable year are deducted in that year. Disallowed business interest expense carryforwards are deducted in the order of the taxable years in which they arose, beginning with the earliest taxable year, subject to certain limitations (for example, the limitation under section 382). For purposes of section 163(j), disallowed disqualified interest is treated as carried forward from the taxable year in which a deduction was disallowed under old section 163(j).

(3) *Consolidated groups*—(i) *In general.* A consolidated group's disallowed business interest expense carryforwards for the current consolidated return year (the current year) are the carryforwards from the group's prior consolidated return years plus any carryforwards from separate return years.

(ii) *Deduction of business interest expense*—(A) *General rule.* All current-year business interest expense of members of a consolidated group is deducted in the current year before any disallowed business interest expense carryforwards from prior taxable years are deducted in the current year. Disallowed business interest expense carryforwards from prior taxable years are deducted in the order of the taxable years in which they arose, beginning with the earliest taxable year, subject to the limitations described in this section.

(B) *Section 163(j) limitation equals or exceeds the current-year business interest expense and disallowed business interest expense carryforwards from prior taxable years.* If a consolidated group's section 163(j) limitation for the current year equals or exceeds the aggregate amount of its members' current-year business interest expense and disallowed business interest expense carryforwards from prior taxable years that are available for deduction, then none of the current-year business interest expense or disallowed business interest expense carryforwards is subject to disallowance in the current year under section 163(j). However, a deduction for the members' business interest expense may be subject to limitation under other provisions of the Code or the Income Tax Regulations (see, for example, paragraphs (c), (d), (e), and (f) of this section).

(C) *Current-year business interest expense and disallowed business interest expense carryforwards exceed section 163(j) limitation.* If the aggregate amount of members' current-year business interest expense and disallowed business interest expense carryforwards from prior taxable years exceeds the consolidated group's section 163(j) limitation for the current year, then the following rules apply in the order provided:

(*1*) The group first determines whether its section 163(j) limitation for the current year equals or exceeds the aggregate amount of the members' current-year business interest expense.

(*i*) If the group's section 163(j) limitation for the current year equals or exceeds the aggregate amount of the members' current-year business interest expense, then no amount of the group's current-year business interest expense is subject to disallowance in the current year under section 163(j). Once the group has taken into account its members' current-year business interest expense, the group applies the rules of paragraph (b)(3)(ii)(C)(*4*) of this section.

(*ii*) If the aggregate amount of members' current-year business interest expense exceeds the group's section 163(j) limitation for the current year, then the group applies the rule in paragraph (b)(3)(ii)(C)(*2*) of this section.

(*2*) If this paragraph (b)(3)(ii)(C)(*2*) applies (see paragraph (b)(3)(ii)(C)(*1*)(*ii*) of this section), then each member with current-year business interest expense and with current-year business interest income or floor plan financing interest expense deducts current-year business interest expense in an amount that does not exceed the sum of the member's business interest income and floor plan financing interest expense for the current year.

(*3*) After applying the rule in paragraph (b)(3)(ii)(C)(*2*) of this section, if the group has any section 163(j) limitation remaining for the current year, then each member with remaining current-year business interest expense deducts a portion of its expense based on its allocable share of the consolidated group's remaining section 163(j) limitation.

(*4*) If this paragraph (b)(3)(ii)(C)(*4*) applies (see paragraph (b)(3)(ii)(C)(*1*)(*i*) of this section), and if the group has any section 163(j) limitation remaining for the current year after applying the rules in paragraph (b)(3)(ii)(C)(*1*) of this section, then disallowed business interest expense carryforwards permitted to be deducted (including under paragraph (d)(1)(A) of this section) in the current year are to be deducted in the order of the taxable years in which they arose, beginning with the earliest taxable year. Disallowed business interest expense carryforwards from taxable years ending on the same date that are available to offset tentative taxable income for the current year generally are to be deducted on a pro rata basis under the principles of paragraph (b)(3)(ii)(C)(*3*) of this section. For example, assume that P and S are the only members of a consolidated group with a section 163(j) limitation for the current year (Year 2) of $200x; the amount of current-year business interest expense deducted in Year 2 is $100x; and P and S, respectively, have $140x and $60x of disallowed business interest expense carryforwards from Year 1 that are not subject to limitation under paragraph (c), (d), or (e) of this section. Under these facts, P would be allowed to deduct $70x of its carryforwards from Year 1 ($100x × ($140x/($60x + $140x)) = $70x), and S would be allowed to deduct $30x of its carryforwards from Year 1 ($100x × ($60x/($60x + $140x)) = $30x). But see § 1.383–1(d)(1)(ii), providing that, if losses subject to and not subject to the section 382 limitation are carried from the same taxable year, losses subject to the limitation are deducted before losses not subject to the limitation.

(*5*) Each member with remaining business interest expense after applying the rules of this paragraph (b)(3)(ii), taking into account the limitations in paragraphs (c), (d), (e), and (f) of this section, carries the expense forward to the succeeding taxable year as a disallowed business interest expense carryforward under section 163(j)(2) and § 1.163(j)–2(c).

(iii) *Departure from group.* If a corporation ceases to be a member during a consolidated return year, the corporation's current-year business interest expense from the taxable period ending on the day of the corporation's change in status as a member, as well as the corporation's disallowed business interest expense carryforwards from prior taxable years that are available to offset tentative taxable income in the consolidated return year, are first made available for deduction during that consolidated return year. See § 1.1502–76(b)(1)(i); see also § 1.1502–36(d) (regarding reductions of deferred deductions on the transfer of loss shares of subsidiary stock). Only the amount that is neither deducted by the group in that consolidated return year nor otherwise reduced under the Code or regulations may be carried to the corporation's first separate return year after its change in status.

(iv) *Example: Deduction of interest expense*—(A) *Facts.* (*1*) P wholly owns A, which is a member of the consolidated group of which P is the common parent. P and A each borrow money from Z, an unrelated third party. The business interest expense of P and A in Years 1, 2, and 3, and the P group's section 163(j) limitation for those years, are as follows:

TABLE 1 TO PARAGRAPH (b)(3)(iv)(A)(*1*)

Year	P's business interest expense	A's business interest expense	P group's section 163(j) limitation
1	$150x	$50x	$100x
2	60x	90x	120x
3	25x	50x	185x

(*2*) P and A have neither business interest income nor floor plan financing interest expense in Years 1, 2, and 3. Additionally, the P group is neither eligible for the small business exemption in § 1.163(j)–2(d) nor engaged in an excepted trade or business.

(B) *Analysis*—(*1*) *Year 1.* In Year 1, the aggregate amount of the P group members' current-year business interest expense ($150x + $50x) exceeds the P group's section 163(j) limitation ($100x). As a result, the rules of paragraph (b)(3)(ii)(C) of this section apply. Because the P group members' current-year business interest expense exceeds the group's section 163(j) limitation for Year 1, P and A must apply the rule in paragraph (b)(3)(ii)(C)(*2*) of this section. Pursuant to paragraph (b)(3)(ii)(C)(*2*) of this section, each of P and A must deduct its current-year business interest expense to the extent of its business interest income and floor plan financing interest expense. Neither P nor A has business interest income or floor plan financing interest expense in Year 1. Next, pursuant to paragraph (b)(3)(ii)(C)(*3*) of this section, each of P and A must deduct a portion of its current-year business interest expense based on its allocable share of the consolidated group's remaining section 163(j) limitation ($100x). P's allocable share is $75x ($100x × ($150x/$200x) = $75x), and A's allocable share is $25x ($100x × ($50x/$200x) = $25x). Accordingly, in Year 1, P deducts $75x of its current-year business interest expense, and A deducts $25x of its current-year business interest expense. P has a disallowed business interest expense carryforward from Year 1 of $75x ($150x − $75x = $75x), and A has a disallowed business interest expense carryforward from Year 1 of $25x ($50x − $25x = $25x).

(*2*) *Year 2.* In Year 2, the aggregate amount of the P group members' current-year business interest expense ($60x + $90x) and disallowed business interest expense carryforwards ($75x + $25x) exceeds the P group's section 163(j) limitation ($120x). As a result, the rules of paragraph (b)(3)(ii)(C) of this section apply. Because the P group members' current-year business interest expense exceeds the group's section 163(j) limitation for Year 2, P and A must apply the rule in paragraph (b)(3)(ii)(C)(*2*) of this section. Pursuant to paragraph (b)(3)(ii)(C)(*2*) of this section, each of P and A must deduct its current-year business interest expense to the extent of its business interest income and floor plan financing interest expense. Neither P nor A has business interest income or floor plan financing interest expense in Year 2. Next, pursuant to paragraph (b)(3)(ii)(C)(*3*) of this section, each of P and A must deduct a portion of its current-year business interest expense based on its allocable share of the consolidated group's remaining section 163(j) limitation ($120x). P's allocable share is $48x (($120x × ($60x/$150x)) = $48x), and A's allocable share is $72x (($120x × ($90x/$150x)) = $72x). Accordingly, in Year 2, P deducts $48x of current-year business interest expense, and A deducts $72x of current-year business interest expense. P has a disallowed business interest expense carryforward from Year 2 of $12x ($60x − $48x = $12x), and A has a disallowed business interest expense carryforward from Year 2 of $18x ($90x − $72x = $18x). Additionally, because the P group has no section 163(j) limitation remaining after deducting current-year business interest expense in Year 2, the full amount of P and A's disallowed business interest expense carryforwards from Year 1 ($75x and $25x, respectively) also are carried forward to Year 3. As a result, at the beginning of Year 3, P and A's respective disallowed business interest expense carryforwards are as follows:

TABLE 2 TO PARAGRAPH (b)(3)(iv)(B)(*2*)

	Year 1 disallowed business interest expense carryforwards	Year 2 disallowed business interest expense carryforwards	Total disallowed business interest expense carryforwards
P	$75x	$12x	$87x
A	25x	18x	43x

TABLE 2 TO PARAGRAPH (b)(3)(iv)(B)(*2*)—Continued

	Year 1 disallowed business interest expense carryforwards	Year 2 disallowed business interest expense carryforwards	Total disallowed business interest expense carryforwards
Total	100x	30x	130x

(*3*) *Year 3.* In Year 3, the aggregate amount of the P group members' current-year business interest expense ($25x + $50x = $75x) and disallowed business interest expense carryforwards ($130x) exceeds the P group's section 163(j) limitation ($185x). As a result, the rules of paragraph (b)(3)(ii)(C) of this section apply. Because the P group's section 163(j) limitation for Year 3 equals or exceeds the P group members' current-year business interest expense, no amount of the members' current-year business interest expense is subject to disallowance under section 163(j) (see paragraph (b)(3)(ii)(C)(*1*) of this section). After each of P and A deducts its current-year business interest expense, the P group has $110x of section 163(j) limitation remaining for Year 3 ($185x − $25x − $50x = $110x). Next, pursuant to paragraph (b)(3)(ii)(C)(*4*) of this section, $110x of disallowed business interest expense carryforwards are deducted on a pro rata basis, beginning with carryforwards from Year 1. Because the total amount of carryforwards from Year 1 ($100x) is less than the section 163(j) limitation remaining after the deduction of Year 3 business interest expense ($110x), all of the Year 1 carryforwards are deducted in Year 3. After current-year business interest expense and Year 1 carryforwards are deducted, the P group's remaining section 163(j) limitation in Year 3 is $10x. Because the Year 2 carryforwards ($30x) exceed the remaining section 163(j) limitation ($10x), under paragraph (b)(3)(ii)(C)(*4*) of this section, each of P and A will deduct a portion of its Year 2 carryforwards based on its allocable share of the consolidated group's remaining section 163(j) limitation. P's allocable share is $4x (($10x × ($12x/$30x)) = $4x), and A's allocable share is $6x (($10x × ($18x/$30x)) = $6x). Accordingly, P and A may deduct $4x and $6x, respectively, of their Year 2 carryforwards. For Year 4, P and A have $8x and $12x of disallowed business interest expense carryforwards from Year 2, respectively.

(c) *Disallowed business interest expense carryforwards in transactions to which section 381(a) applies.* For rules governing the application of section 381(c)(20) to disallowed business interest expense carryforwards, including limitations on an acquiring corporation's use of the disallowed business interest expense carryforwards of the transferor or distributor corporation in the acquiring corporation's first taxable year ending after the date of distribution or transfer, see § 1.381(c)(20)–1.

(d) *Limitations on disallowed business interest expense carryforwards from separate return limitation years*—(1) *General rule*—(A) *Cumulative section 163(j) SRLY limitation.* This paragraph (d) applies to disallowed business interest expense carryforwards of a member arising in a SRLY (see § 1.1502–1(f))) or treated as arising in a SRLY under the principles of § 1.1502–21(c) and (g). The amount of the carryforwards described in the preceding sentence that are included in the consolidated group's business interest expense deduction for any taxable year under paragraph (b) of this section may not exceed the aggregate section 163(j) limitation for all consolidated return years of the group, determined by reference only to the member's items of income, gain, deduction, and loss, and reduced (including below zero) by the member's business interest expense (including disallowed business interest expense carryforwards) absorbed by the group in all consolidated return years (cumulative section 163(j) SRLY limitation). For purposes of computing the member's cumulative section 163(j) SRLY limitation, intercompany items referred to in § 1.163(j)–4(d)(2)(iv) are included, with the exception of interest items with regard to intercompany obligations. See § 1.163(j)–4(d)(2)(v). Thus, for purposes of this paragraph (d), income and expense items arising from intercompany transactions (other than interest income and expense with regard to intercompany obligations) are included in the calculation of the cumulative section 163(j) SRLY limitation. In addition, items of interest expense with regard to intercompany obligations are not characterized as business interest expense for purposes of the reduction described in the second sentence of this paragraph (d)(1)(A).

(B) *Subgrouping.* For purposes of this paragraph (d), the SRLY subgroup principles of § 1.1502–21(c)(2)(i) (with regard to carryovers of SRLY losses) apply with appropriate adjustments.

(2) *Deduction of disallowed business interest expense carryforwards arising in a SRLY.* Notwithstanding paragraph (d)(1) of this section, disallowed business interest expense carryforwards of a member arising in a SRLY are available for deduction by the consolidated group in the current year only to the extent the group has remaining section 163(j) limitation for the current year after the deduction of current-year business interest expense and disallowed business interest expense carryforwards from earlier taxable years that are permitted to be deducted in the current year (see paragraph (b)(3)(ii)(A) of this section). SRLY-limited disallowed business interest expense carryforwards are deducted on a pro rata basis (under the principles of paragraph (b)(3)(ii)(C)(*3*) of this section) with non-SRLY limited disallowed business interest expense carryforwards from taxable years ending on the same date. See also § 1.1502–21(b)(1).

(3) *Examples.* The principles of this paragraph (d) are illustrated by the following examples. For purposes of the examples in this paragraph (d)(3), unless otherwise stated, P, R, S, and T are taxable domestic C corporations that are not RICs or REITs and that file their tax returns on a calendar-year basis; none of P, R, S, or T qualifies for the small business exemption under section 163(j)(3) or is engaged in an excepted trade or business; all interest expense is deductible except for the potential application of section 163(j); and the facts set forth the only corporate activity.

(i) *Example 1: Determination of SRLY limitation*—(A) *Facts.* Individual A owns P. In 2021, A forms T, which pays or accrues a $100x business interest expense for which a deduction is disallowed under section 163(j) and that is carried forward to 2022. P does not pay or accrue business interest expense in 2021, and P has no disallowed business interest expense carryforwards from prior taxable years. At the close of 2021, P acquires all of the stock of T, which joins with P in filing a consolidated return beginning in 2022. Neither P nor T pays or accrues business interest expense in 2022, and the P group has a section 163(j) limitation of $300x in that year. This limitation would be $70x if determined by reference solely to T's items for all consolidated return years of the P group.

(B) *Analysis.* T's $100x of disallowed business interest expense carryforwards from 2021 arose in a SRLY. P's acquisition of T was not an ownership change as defined by section 382(g); thus, T's disallowed business interest expense carryforwards are subject to the SRLY limitation in paragraph (d)(1) of this section. T's cumulative section 163(j) SRLY limitation for 2022 is the P group's section 163(j) limitation, determined by reference solely to T's items for all consolidated return years of the P group ($70x). See paragraph (d)(1) of this section. Thus, $70x of T's disallowed business interest expense carryforwards are available to be deducted by the P group in 2022, and the remaining $30x of T's disallowed business interest expense carryforwards are carried forward to 2023. After the P group deducts $70x of T's disallowed business interest expense carryforwards, T's cumulative section 163(j) SRLY limitation is reduced by $70x to $0.

(C) *Cumulative section 163(j) SRLY limitation of $0.* The facts are the same as in *Example 1* in paragraph (d)(3)(i)(A) of this section, except that T's cumulative section 163(j) SRLY limitation for 2022 is $0. Because the amount of T's disallowed business interest expense carryforwards that may be deducted by the P group in 2022 may not exceed T's cumulative section 163(j) SRLY limitation, none of T's carryforwards from 2021 may be deducted by the P group in 2022. Because none of T's disallowed business interest expense carryforwards are absorbed by the P group in 2022, T's cumulative section 163(j) SRLY limitation remains at $0 entering 2023.

(ii) *Example 2: Cumulative section 163(j) SRLY limitation less than zero*—(A) *Facts.* P and S are the only members of a consolidated group. P has neither current-year business interest expense nor disallowed business interest expense carryforwards. For the current year, the P group has a section 163(j) limitation of $150x, $25x of which is attributable to P, and $125x of which is attributable to S. S has $100x of disallowed business interest expense carryforwards that arose in a SRLY and $150x of current-year business interest expense. S's cumulative section 163(j) SRLY limitation entering the current year (computed by reference solely to S's items for all consolidated return years of the P group) is $0.

(B) *Analysis.* Under paragraph (d)(1) of this section, S's cumulative section 163(j) SRLY limitation is increased by $125x to reflect S's tax items for the current year. The P group's section 163(j) limitation permits the P group to deduct all $150x of S's current-year business interest expense. S's cumulative section 163(j) SRLY limitation is reduced by the $150x of S's business interest expense absorbed by the P group in the current year, which results in a −$25x balance. Thus, none of S's SRLY'd disallowed business interest expense carryforwards may be deducted by the P group in the current year. Entering the subsequent year, S's cumulative section 163(j) SRLY limitation remains −$25x.

(iii) *Example 3: Pro rata absorption of SRLY-limited disallowed business interest expense carryforwards*—(A) *Facts.* P, R, and S are the only members of a consolidated group, and no member has floor plan financing or business interest income. P has $60x of current-year business interest expense and $40x of disallowed business interest expense carryforwards from the previous year, which was not a separate return year. R has $120x of current-year business interest expense and $80x of disallowed business interest expense carryforwards from the previous year, which was not a separate return year. S has $70x of current-year business interest expense and $30x of disallowed business interest expense carryforwards from the previous year, which was a separate return year. The P group has a section 163(j) limitation of $300x, $50x of which is attributable to P, $90x to R, and $160x to S. S's cumulative section 163(j) SRLY limitation entering the current year (computed by reference solely to S's items for all consolidated return years of the P group) is $0.

TABLE 3 TO PARAGRAPH (d)(3)(iii)(A)

	Current-year business interest expense	Disallowed business interest expense carryforwards from prior taxable year	Section 163(j) limitation
P	$60x	$40x	$50x
R	120x	80x	90x
S	70x	(SRLY) 30x	160x
Total	250x	150x	300x

(B) *Analysis.* Under paragraph (d)(1) of this section, S's cumulative section 163(j) SRLY limitation is increased in the current year by $160x. The P group's section 163(j) limitation permits the P group to deduct all $70x of S's current-year business interest expense (and all $180x of P and R's current-year business interest expense). S's cumulative section 163(j) SRLY limitation is reduced by the $70x of S's business interest expense absorbed by the P group in the current year, resulting in a $90x balance. Because the P group has $50x of section 163(j) limitation remaining after the absorption of current-year business interest expense, the P group can absorb $50x of its members' disallowed business interest expense carryforwards. Under paragraph (d)(2) of this section, SRLY-limited disallowed business interest expense carryforwards are deducted on a pro rata basis with other disallowed business interest expense carryforwards from the same taxable year. Accordingly, the P group can deduct $10x ($50x × ($30x/$150x)) of S's SRLY-limited disallowed business interest expense carryforwards. S's cumulative section 163(j) SRLY limitation is reduced (to $80x) by the $10x of SRLY-limited disallowed business interest carryforwards absorbed by the P group in the current year.

(C) *Cumulative section 163(j) SRLY limitation of −$75x.* The facts are the same as in *Example 3* in paragraph (d)(3)(iii)(A) of this section, except that S's cumulative section 163(j) SRLY limitation entering the current year is −$75x. After adjusting for S's tax items for the current year ($160x) and the P group's absorption of S's current-year business interest expense ($70x), S's cumulative section 163(j) SRLY limitation is $15x (−$75x + $160x − $70x). Because S's cumulative section 163(j) SRLY limitation ($15x) is less than the amount of S's SRLY-limited disallowed business interest expense carryforwards ($30x), the pro rata calculation under paragraph (d)(2) of this section is applied to $15x (rather than $30x) of S's carryforwards. Accordingly, the P group can deduct $5.56x ($50x × ($15x/$135x)) of S's SRLY-limited disallowed business interest expense carryforwards. S's cumulative section 163(j) SRLY limitation is reduced (to $9.44x) by the $5.56x of SRLY-limited disallowed business interest carryforwards absorbed by the P group in the current year.

(e) *Application of section 382*—(1) *Pre-change loss.* For rules governing the treatment of a disallowed business interest expense as a pre-change loss for purposes of section 382, see §§ 1.382–2(a) and 1.382–6. For rules governing the application of section 382 to disallowed disqualified interest carryforwards, see § 1.163(j)–11(c)(4).

(2) *Loss corporation.* For rules governing when a disallowed business interest expense causes a corporation to be a loss corporation within the meaning of section 382(k)(1), see § 1.382–2(a). For the application of section 382 to disallowed disqualified interest carryforwards, see § 1.163(j)–11(c)(4).

(3) *Ordering rules for utilization of pre-change losses and for absorption of the section 382 limitation.* For ordering rules for the utilization of disallowed business interest expense, net operating losses, and other pre-change losses, and for the absorption of the section 382 limitation, see § 1.383–1(d).

(4) *Disallowed business interest expense from the pre-change period in the year of a testing date.* For rules governing the treatment of disallowed business interest expense from the pre-change period (within the meaning of § 1.382–6(g)(2)) in the year of a testing date, see § 1.382–2.

(5) *Recognized built-in loss.* For a rule providing that a section 382 disallowed business interest carryforward (as defined in § 1.382–2(a)(7)) is not treated as a recognized built-in loss for purposes of section 382, see § 1.382–7(d)(5).

(f) *Overlap of SRLY limitation with section 382.* For rules governing the overlap of the application of section 382 and the application of the SRLY rules, see § 1.1502–21(g).

(g) *Additional limitations.* Additional rules provided under the Code or regulations also apply to limit the use of disallowed business interest expense carryforwards. For rules governing the relationship between section 163(j) and other provisions affecting the deductibility of interest, see § 1.163(j)–3.

(h) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

§ 1.163(j)–6 Application of the section 163(j) limitation to partnerships and subchapter S corporations.

(a) *Overview.* If a deduction for business interest expense of a partnership or an S corporation is subject to the section 163(j) limitation, section 163(j)(4) provides that the section 163(j) limitation applies at the partnership or S corporation level and any deduction for business interest expense is taken into account in determining the nonseparately stated taxable income or loss of the partnership or S corporation. Once a partnership or an S corporation determines its business interest expense, business interest income, ATI, and floor plan financing interest expense, the partnership or S corporation calculates its section 163(j) limitation by applying the rules of § 1.163(j)–2(b) and this section. Paragraph (b) of this section provides definitions used in this section. Paragraph (c) of this section provides rules regarding the character of a partnership's deductible business interest expense and excess business interest expense. Paragraph (d) of this section provides rules regarding the calculation of a partnership's ATI and floor plan financing interest expense. Paragraph (e) of this section provides rules regarding a partner's ATI and business interest income. Paragraph (f) of this section provides an eleven-step computation necessary for properly allocating a partnership's deductible business interest expense and section 163(j) excess items to its partners. Paragraph (g) of this section applies carryforward rules at the partner level if a partnership has excess business interest expense. Paragraph (h) of this section provides basis adjustment rules, and paragraph (k) of this section provides rules regarding investment items of a partnership. Paragraph (l) of this section provides rules regarding S corporations. Paragraph (m) of this section provides rules for partnerships and S corporations not subject to section 163(j). Paragraph (o) of this section provides examples illustrating the rules of this section.

(b) *Definitions.* In addition to the definitions contained in § 1.163(j)–1, the following definitions apply for purposes of this section.

(1) *Section 163(j) items.* The term *section 163(j) items* means the partnership or S corporation's business interest expense, business interest income, and items comprising ATI.

(2) *Partner basis items.* The term *partner basis items* means any items of income, gain, loss, or deduction resulting from either an adjustment to the basis of partnership property used in a non-excepted trade or business made pursuant to section 743(b) or the operation of section 704(c)(1)(C)(i) with respect to such property. Partner basis items also include section 743(b) basis adjustments used to increase or decrease a partner's share of partnership gain or loss on the sale of partnership property used in a non-excepted trade or business (as described in § 1.743–1(j)(3)(i)) and amounts resulting from the operation of section 704(c)(1)(C)(i) used to decrease a partner's share of partnership gain or increase a partner's share of partnership loss on the sale of such property.

(3) *Remedial items.* The term *remedial items* means any allocation to a partner of remedial items of income, gain, loss, or deduction pursuant to section 704(c) and § 1.704–3(d).

(4) *Excess business interest income.* The term *excess business interest income* means the amount by which a partnership's or S corporation's business interest income exceeds its

business interest expense in a taxable year.

(5) *Deductible business interest expense.* The term *deductible business interest expense* means the amount of a partnership's or S corporation's business interest expense that is deductible under section 163(j) in the current taxable year following the application of the limitation contained in § 1.163(j)–2(b).

(6) *Section 163(j) excess items.* The term *section 163(j) excess items* means the partnership's excess business interest expense, excess taxable income, and excess business interest income.

(7) *Non-excepted assets.* The term *non-excepted assets* means assets from a non-excepted trade or business.

(8) *Excepted assets.* The term *excepted assets* means assets from an excepted trade or business.

(c) *Business interest income and business interest expense of a partnership*—

(1)–(2) [Reserved]

(3) *Character of business interest expense.* If a partnership has deductible business interest expense, such deductible business interest expense is not subject to any additional application of section 163(j) at the partner-level because it is taken into account in determining the nonseparately stated taxable income or loss of the partnership. However, for all other purposes of the Code, deductible business interest expense and excess business interest expense retain their character as business interest expense at the partner-level. For example, for purposes of section 469, such business interest expense retains its character as either passive or non-passive in the hands of the partner. Additionally, for purposes of section 469, deductible business interest expense and excess business interest expense from a partnership remain interest derived from a trade or business in the hands of a partner even if the partner does not materially participate in the partnership's trade or business activity. For additional rules regarding the interaction between sections 465, 469, and 163(j), see § 1.163(j)–3.

(d) *Adjusted taxable income of a partnership*—(1) *Tentative taxable income of a partnership.* For purposes of computing a partnership's ATI under § 1.163(j)–1(b)(1), the tentative taxable income of a partnership is the partnership's taxable income determined under section 703(a), but computed without regard to the application of the section 163(j) limitation.

(2) *Section 734(b), partner basis items, and remedial items.* A partnership takes into account items resulting from adjustments made to the basis of its property pursuant to section 734(b) for purposes of calculating its ATI pursuant to § 1.163(j)–1(b)(1). However, partner basis items and remedial items are not taken into account in determining a partnership's ATI under § 1.163(j)–1(b)(1). Instead, partner basis items and remedial items are taken into account by the partner in determining the partner's ATI pursuant to § 1.163(j)–1(b)(1). See *Example 6* in paragraph (o)(6) of this section.

(e) *Adjusted taxable income and business interest income of partners*—(1) *Modification of adjusted taxable income for partners.* The ATI of a partner in a partnership generally is determined in accordance with § 1.163(j)–1(b)(1), without regard to such partner's distributive share of any items of income, gain, deduction, or loss of such partnership, except as provided for in paragraph (m) of this section, and is increased by such partner's distributive share of such partnership's excess taxable income determined under paragraph (f) of this section. For rules regarding corporate partners, see § 1.163(j)–4(b)(3).

(2) *Partner basis items and remedial items.* Partner basis items and remedial items are taken into account as items derived directly by the partner in determining the partner's ATI for purposes of the partner's section 163(j) limitation. If a partner is allocated remedial items, such partner's ATI is increased or decreased by the amount of such items. Additionally, to the extent a partner is allocated partner basis items, such partner's ATI is increased or decreased by the amount of such items. See *Example 6* in paragraph (o)(6) of this section.

(3) *Disposition of partnership interests.* If a partner recognizes gain or loss upon the disposition of interests in a partnership, and the partnership in which the interest is being disposed owns only non-excepted trade or business assets, the gain or loss on the disposition of the partnership interest is included in the partner's ATI. See § 1.163(j)–10(b)(4)(ii) for dispositions of interests in partnerships that own—

(i) Non-excepted assets and excepted assets; or

(ii) Investment assets; or

(iii) Both.

(4) *Double counting of business interest income and floor plan financing interest expense prohibited.* For purposes of calculating a partner's section 163(j) limitation, the partner does not include—

(i) Business interest income from a partnership that is subject to section 163(j), except to the extent the partner is allocated excess business interest income from that partnership pursuant to paragraph (f)(2) of this section; and

(ii) The partner's allocable share of the partnership's floor plan financing interest expense, because such floor plan financing interest expense already has been taken into account by the partnership in determining its nonseparately stated taxable income or loss for purposes of section 163(j).

(f) *Allocation and determination of section 163(j) excess items made in the same manner as nonseparately stated taxable income or loss of the partnership*—(1) *Overview*—(i) *In general.* The purpose of this paragraph is to provide guidance regarding how a partnership must allocate its deductible business interest expense and section 163(j) excess items, if any, among its partners. For purposes of section 163(j)(4) and this section, allocations and determinations of deductible business interest expense and section 163(j) excess items are considered made in the same manner as the nonseparately stated taxable income or loss of the partnership if, and only if, such allocations and determinations are made in accordance with the eleven-step computation set forth in paragraphs (f)(2)(i) through (xi) of this section. A partnership first determines its section 163(j) limitation, total amount of deductible business interest expense, and section 163(j) excess items under paragraph (f)(2)(i) of this section. The partnership then applies paragraphs (f)(2)(ii) through (xi) of this section, in that order, to determine how those items of the partnership are allocated among its partners. At the conclusion of the eleven-step computation set forth in paragraphs (f)(2)(i) through (xi) of this section, the total amount of deductible business interest expense and section 163(j) excess items allocated to each partner will equal the partnership's total amount of deductible business interest expense and section 163(j) excess items.

(ii) *Relevance solely for purposes of section 163(j).* No rule set forth in paragraph (f)(2) of this section prohibits a partnership from making an allocation to a partner of any item of partnership income, gain, loss, or deduction that is otherwise permitted under section 704 and the regulations under section 704 of the Code. Accordingly, any calculations in paragraphs (f)(2)(i) through (xi) of this section are solely for the purpose of determining each partner's deductible business interest expense and section 163(j) excess items and do not otherwise affect any other provision under the Code, such as section 704(b). Additionally, floor plan financing interest expense is not allocated in accordance with paragraph (f)(2) of this section. Instead, floor plan financing interest expense of a partnership is allocated to its partners under section 704(b) and is taken into account as a nonseparately stated item of loss for purposes of section 163(j).

(2) *Steps for allocating deductible business interest expense and section 163(j) excess items*—(i) *Partnership-level calculation required by section 163(j)(4)(A).* First, a partnership must determine its section 163(j) limitation pursuant to § 1.163(j)–2(b). This calculation determines a partnership's total amounts of excess business interest income, excess taxable income, excess business interest expense (that is, the partnership's section 163(j) excess items), and deductible business interest expense under section 163(j) for a taxable year.

(ii) *Determination of each partner's relevant section 163(j) items.* Second, a partnership must determine each partner's allocable share of each section 163(j) item under section 704(b) and the regulations under section 704 of the Code, including any allocations under section 704(c), other than remedial items. Only section 163(j) items that were actually taken into account in the partnership's section 163(j) calculation under paragraph (f)(2)(i) of this section are taken into account for purposes of this paragraph (f)(2)(ii). Partner basis items, allocations of investment income and expense, remedial items, and amounts determined for the partner under § 1.163–8T are not taken into account for purposes of this paragraph (f)(2)(ii). For purposes of paragraphs (f)(2)(ii) through (xi) of this section, the term *allocable ATI* means a partner's distributive share of the partnership's ATI (that is, a partner's distributive share of gross income and gain items comprising ATI less such partner's distributive share of gross loss and deduction items comprising ATI), the term *allocable business interest income* means a partner's distributive share of the partnership's business interest income, and the term *allocable business interest expense* means a partner's distributive share of the partnership's business interest expense that is not floor plan financing interest expense. If the partnership determines that each partner has a pro rata share of allocable ATI, allocable business interest income, and allocable business interest expense, then the partnership may bypass paragraphs (f)(2)(iii) through (xi) of this section and allocate its section 163(j) excess items in the same proportion. See *Example 1* through *Example 16* in paragraphs (o)(1) through (16), respectively. This pro-rata exception does not result in allocations of section 163(j) excess items that vary from the array of allocations of section 163(j) excess items that would have resulted had paragraphs (f)(2)(iii) through (xi) been applied.

(iii) *Partner-level comparison of business interest income and business interest expense.* Third, a partnership must compare each partner's allocable business interest income to such partner's allocable business interest expense. Paragraphs (f)(2)(iii) through (v) of this section determine how a partnership must allocate its excess business interest income among its partners, as well as the amount of each partner's allocable business interest expense that is not deductible business interest expense after taking the partnership's business interest income into account. To the extent a partner's allocable business interest income exceeds its allocable business interest expense, the partner has an *allocable business interest income excess.* The aggregate of all the partners' allocable business interest income excess amounts is the *total allocable business interest income excess.* To the extent a partner's allocable business interest expense exceeds its allocable business interest income, the partner has an *allocable business interest income deficit.* The aggregate of all the partners' allocable business interest income deficit amounts is the *total allocable business interest income deficit.* These amounts are required to perform calculations in paragraphs (f)(2)(iv) and (v) of this section, which appropriately reallocate allocable business interest income excess to partners with allocable business interest income deficits in order to reconcile the partner-level calculation under paragraph (f)(2)(iii) of this section with the partnership-level result under paragraph (f)(2)(i) of this section.

(iv) *Matching partnership and aggregate partner excess business interest income.* Fourth, a partnership must determine each partner's final allocable business interest income excess. A partner's *final allocable business interest income excess* is determined by reducing, but not below zero, such partner's allocable business interest income excess (if any) by the partner's step four adjustment amount. A partner's *step four adjustment amount* is the product of the total allocable business interest income deficit and the ratio of such partner's allocable business interest income excess to the total allocable business interest income excess. The rules of this paragraph (f)(2)(iv) ensure that, following the application of paragraph (f)(2)(xi) of this section, the aggregate of all the partners' allocations of excess business interest income equals the total amount of the partnership's excess business interest income as determined in paragraph (f)(2)(i) of this section.

(v) *Remaining business interest expense determination.* Fifth, a partnership must determine each partner's remaining business interest expense. A partner's *remaining business interest expense* is determined by reducing, but not below zero, such partner's allocable business interest income deficit (if any) by such partner's step five adjustment amount. A partner's *step five adjustment amount* is the product of the total allocable business interest income excess and the ratio of such partner's allocable business interest income deficit to the total allocable business interest income deficit. Generally, a partner's remaining business interest expense is a partner's allocable business interest income deficit adjusted to reflect a reallocation of allocable business interest income excess from other partners. Determining a partner's remaining business interest expense is necessary to perform an ATI calculation that begins in paragraph (f)(2)(vii) of this section.

(vi) *Determination of final allocable ATI.* Sixth, a partnership must determine each partner's final allocable ATI. Paragraphs (f)(2)(vi) through (x) of this section determine how a partnership must allocate its excess taxable income and excess business interest expense among its partners.

(A) *Positive allocable ATI.* To the extent a partner's income and gain items comprising its allocable ATI exceed its deduction and loss items comprising its allocable ATI, the partner has *positive allocable ATI.* The aggregate of all the partners' positive allocable ATI amounts is the *total positive allocable ATI.*

(B) *Negative allocable ATI.* To the extent a partner's deduction and loss items comprising its allocable ATI exceed its income and gain items comprising its allocable ATI, the partner has negative allocable ATI. The aggregate of all the partners' negative allocable ATI amounts is the *total negative allocable ATI.*

(C) *Final allocable ATI.* Any partner with a negative allocable ATI, or an allocable ATI of $0, has a positive allocable ATI of $0. Any partner with a positive allocable ATI of $0 has a final allocable ATI of $0. The final allocable ATI of any partner with a positive allocable ATI greater than $0 is such partner's positive allocable ATI reduced, but not below zero, by the partner's step six adjustment amount. A partner's *step six adjustment amount* is the product of the total negative allocable ATI and the ratio of such partner's positive allocable ATI to the total positive allocable ATI. The total of the partners' final allocable ATI amounts must equal the partnership's ATI amount used to compute its section 163(j) limitation pursuant to § 1.163(j)–2(b).

(vii) *Partner-level comparison of 30 percent of adjusted taxable income and remaining business interest expense.* Seventh, a partnership must compare each partner's ATI capacity to such partner's remaining business interest expense as determined under paragraph (f)(2)(v) of this section. A partner's *ATI capacity* is the amount that is 30 percent of such partner's final allocable ATI as determined under paragraph (f)(2)(vi) of this section. A partner's final allocable ATI is grossed down to 30 percent prior to being compared to its remaining business interest expense in this calculation to parallel the partnership's adjustment to its ATI under section 163(j)(1)(B). To the extent a partner's ATI capacity exceeds its remaining business interest expense, the partner has an *ATI capacity excess.* The aggregate of all the partners' ATI capacity excess amounts is the *total ATI capacity excess.* To the extent a partner's remaining business interest expense exceeds its ATI capacity, the partner has an *ATI capacity deficit.* The aggregate of all the partners' ATI capacity deficit amounts is the *total ATI capacity deficit.* These amounts (which may be subject to adjustment under paragraph (f)(2)(viii) of this section) are required to perform calculations in paragraphs (f)(2)(ix) and (x) of this section, which appropriately reallocate ATI capacity excess to partners with ATI capacity deficits in order to reconcile the partner-level calculation under paragraph (f)(2)(vii) of this section with the partnership-level result under paragraph (f)(2)(i) of this section.

(viii) *Partner priority right to ATI capacity excess determination.* (A) Eighth, the partnership must determine whether it is required to make any adjustments described in this paragraph (f)(2)(viii) and, if it is, make such adjustments. The rules of this paragraph (f)(2)(viii) are necessary to account for adjustments made to a partner's allocable ATI in paragraph (f)(2)(vi) of this section to ensure that the partners who had a negative allocable ATI do not inappropriately benefit under the rules of paragraphs (f)(2)(ix) through (xi) of this section to the detriment of the partners who had positive allocable ATI. The partnership must perform the calculations and make the necessary adjustments described under paragraphs (f)(2)(viii)(B) and (C) or paragraph (f)(2)(viii)(D) of this section if, and only if, there is—

(*1*) An excess business interest expense amount greater than $0 under paragraph (f)(2)(i) of this section;

(*2*) A total negative allocable ATI amount greater than $0 under paragraph (f)(2)(vi) of this section; and

(*3*) A total ATI capacity excess amount greater than $0 under paragraph (f)(2)(vii) of this section.

(B) A partnership must determine each partner's priority amount and usable priority amount. A partner's *priority amount* is 30 percent of the amount by which a partner's positive allocable ATI under paragraph (f)(2)(vi)(A) of this section exceeds such partner's final allocable ATI under paragraph (f)(2)(vi)(C) of this section. However, only partners with an ATI capacity deficit as determined under paragraph (f)(2)(vii) of this section can have a priority amount greater than $0. The aggregate of all the partners' priority amounts is the *total priority amount.* A partner's *usable priority amount* is the lesser of such partner's priority amount or such partner's ATI capacity deficit as determined under paragraph (f)(2)(vii) of this section. The aggregate of all the partners' usable priority amounts is the *total usable priority amount.* If the total ATI capacity excess amount, as determined under paragraph (f)(2)(vii) of this section, is greater than or equal to the total usable priority amount, then the partnership must perform the adjustments described in paragraph (f)(2)(viii)(C) of this section. If the total usable priority amount is greater than the total ATI capacity excess amount, as determined under paragraph (f)(2)(vii) of this section, then the partnership must perform the adjustments described in paragraph (f)(2)(viii)(D) of this section.

(C) For purposes of paragraph (f)(2)(ix) of this section, each partner's final ATI capacity excess amount is $0. For purposes of paragraph (f)(2)(x) of this section, the following terms have the following meanings for each partner:

(*1*) Each partner's *ATI capacity deficit* is such partner's ATI capacity deficit as determined under paragraph (f)(2)(vii) of this section, reduced by such partner's usable priority amount.

(*2*) The *total ATI capacity deficit* is the total ATI capacity deficit as determined under paragraph (f)(2)(vii) of this section, reduced by the total usable priority amount.

(*3*) The *total ATI capacity excess* is the total ATI capacity excess as determined under paragraph (f)(2)(vii) of this section, reduced by the total usable priority amount.

(D) Any partner with a priority amount greater than $0 is a *priority partner.* Any partner that is not a priority partner is a *non-priority partner.* For purposes of paragraph (f)(2)(ix) of this section, each partner's final ATI capacity excess amount is $0. For purposes of paragraph (f)(2)(x) of this section, each non-priority partner's final ATI capacity deficit amount is such partner's ATI capacity deficit as determined under paragraph (f)(2)(vii) of this section. For purposes of paragraph (f)(2)(x) of this section, the following terms have the following meanings for priority partners.

(*1*) Each priority partner must determine its step eight excess share. A partner's *step eight excess share* is the product of the total ATI capacity excess as determined under paragraph (f)(2)(vii) of this section and the ratio of the partner's priority amount to the total priority amount.

(*2*) To the extent a priority partner's step eight excess share exceeds its ATI capacity deficit as determined under paragraph (f)(2)(vii) of this section, such excess amount is the priority partner's *ATI capacity excess* for purposes of paragraph (f)(2)(x) of this section. The *total ATI capacity excess* is the aggregate of the priority partners' ATI capacity excess amounts as determined under this paragraph (f)(2)(viii)(D)(*2*).

(*3*) To the extent a priority partner's ATI capacity deficit as determined under paragraph (f)(2)(vii) of this section exceeds its step eight excess share, such excess amount is the priority partner's *ATI capacity deficit* for purposes of paragraph (f)(2)(x) of this section. The *total ATI capacity deficit* is the aggregate of the priority partners' ATI capacity deficit amounts as determined under this paragraph (f)(2)(viii)(D)(*3*).

(ix) *Matching partnership and aggregate partner excess taxable income.* Ninth, a partnership must determine each partner's final ATI capacity excess. A partner's *final ATI capacity excess* amount is determined by reducing, but not below zero, such partner's ATI capacity excess (if any) by the partner's step nine adjustment amount. A partner's *step nine adjustment amount* is the product of the total ATI capacity deficit and the ratio of such partner's ATI capacity excess to the total ATI capacity excess. The rules of this paragraph (f)(2)(ix) ensure that, following the application of paragraph (f)(2)(xi) of this section, the aggregate of all the partners' allocations of excess taxable income equals the total amount of the partnership's excess taxable income as determined in paragraph (f)(2)(i) of this section.

(x) *Matching partnership and aggregate partner excess business interest expense.* Tenth, a partnership must determine each partner's final ATI capacity deficit. A partner's *final ATI capacity deficit* amount is determined by reducing, but not below zero, such partner's ATI capacity deficit (if any) by the partner's step ten adjustment amount. A partner's *step ten adjustment amount* is the product of the total ATI capacity excess and the ratio of such partner's ATI capacity deficit to the total ATI capacity deficit. Generally, a partner's final ATI capacity deficit is a partner's ATI capacity deficit adjusted to reflect a reallocation of ATI capacity excess from other partners. The rules of this paragraph (f)(2)(x) ensure that, following the application of paragraph (f)(2)(xi) of this section, the aggregate of all the partners' allocations of excess business interest expense equals the total amount of the partnership's excess business interest expense as determined in paragraph (f)(2)(i) of this section.

(xi) *Final section 163(j) excess item and deductible business interest expense allocation.* Eleventh, a partnership must allocate section 163(j) excess items and deductible business interest expense to its partners. Excess business interest income calculated under paragraph (f)(2)(i) of this section, if any, is allocated dollar for dollar by the partnership to its partners with final allocable business interest income excess amounts. Excess business interest expense calculated under paragraph (f)(2)(i) of this section, if any, is allocated dollar for dollar to partners with final ATI capacity deficit amounts. After grossing up each partner's final ATI capacity excess amount by ten-thirds, excess taxable income calculated under paragraph (f)(2)(i) of this section, if any, is allocated dollar for dollar to partners with final ATI capacity excess amounts. A partner's allocable business interest expense is deductible business interest expense to the extent it exceeds such partner's share of excess business interest expense. See *Example 17* through *Example 21* in paragraphs (o)(17) through (21) of this section, respectively.

(g) *Carryforwards*—(1) *In general.* The amount of any business interest expense not allowed as a deduction to a partnership by reason of § 1.163(j)–2(b) and paragraph (f)(2) of this section for any taxable year is—

(i) Not treated as business interest expense of the partnership in the succeeding taxable year; and

(ii) Subject to paragraph (g)(2) of this section, treated as excess business interest expense, which is allocated to each partner pursuant to paragraph (f)(2) of this section.

(2) *Treatment of excess business interest expense allocated to partners.* If a partner is allocated excess business interest expense from a partnership under paragraph (f)(2) of this section for any taxable year and the excess business interest expense is treated as such under paragraph (h)(2) of this section—

(i) Solely for purposes of section 163(j), such excess business interest expense is treated as business interest expense paid or accrued by the partner in the next succeeding taxable year in which the partner is allocated excess taxable income or excess business interest income from such partnership, but only to the extent of such excess taxable income or excess business interest income; and

(ii) Any portion of such excess business interest expense remaining after the application of paragraph (g)(2)(i) of this section is excess business interest expense that is subject to the limitations of paragraph (g)(2)(i) of this section in succeeding taxable years, unless paragraph (m)(3) of this section applies. See *Example 1* through *Example 16* in paragraphs (o)(1) through (16) of this section, respectively.

(3) *Excess taxable income and excess business interest income ordering rule.* In the event a partner has excess business interest expense from a prior taxable year and is allocated excess taxable income or excess business interest income from the same partnership in a succeeding taxable year, the partner must treat, for purposes of section 163(j), the excess business interest expense as business interest expense paid or accrued by the partner in an amount equal to the partner's share of the partnership's excess taxable income or excess business interest income in such succeeding taxable year. See *Example 2* through *Example 16* in paragraphs (o)(2) through (16) of this section, respectively.

(h) *Basis adjustments*—(1) *Section 704(d) ordering.* Deductible business interest expense and excess business interest expense are subject to section 704(d). If a partner is subject to a limitation on loss under section 704(d) and a partner is allocated losses from a partnership in a taxable year, § 1.704–1(d)(2) requires that the limitation on losses under section 704(d) be apportioned amongst these losses based on the character of each loss (each grouping of losses based on character being a *section 704(d) loss class*). If there are multiple section 704(d) loss classes in a given year, § 1.704–1(d)(2) requires the partner to apportion the limitation on losses under section 704(d) to each section 704(d) loss class proportionately. For purposes of applying this proportionate rule, any deductible business interest expense and business interest expense of an exempt entity (whether allocated to the partner in the current taxable year or suspended under section 704(d) in a prior taxable year), any excess business interest expense allocated to the partner in the current taxable year, and any excess business interest expense from a prior taxable year that was suspended under section 704(d) (negative section 163(j) expense) shall comprise the same section 704(d) loss class. Once the partner determines the amount of limitation on losses apportioned to this section 704(d) loss class, any deductible business interest expense is taken into account before any excess business interest expense or negative section 163(j) expense. See *Example 7* in paragraph (o)(7) of this section.

(2) *Excess business interest expense basis adjustments.* The adjusted basis of a partner in a partnership interest is reduced, but not below zero, by the amount of excess business interest expense allocated to the partner pursuant to paragraph (f)(2) of this section. Negative section 163(j) expense is not treated as excess business interest expense in any subsequent year until such negative section 163(j) expense is no longer suspended under section 704(d). Therefore, negative section 163(j) expense does not affect, and is not affected by, any allocation of excess taxable income to the partner. Accordingly, any excess taxable income allocated to a partner from a partnership while the partner still has negative section 163(j) expense will be included in the partner's ATI. However, once the negative section 163(j) expense is no longer suspended under section 704(d), it becomes excess business interest expense, which is subject to the general rules in paragraph (g) of this section. See *Example 8* in paragraph (o)(8) of this section.

(3) *Partner basis adjustment upon disposition of partnership interest.* If a partner (transferor) disposes of an interest in a partnership, the adjusted basis of the partnership interest being disposed of (transferred interest) is increased immediately before the disposition by the amount of the excess (if any) of the amount of the basis reduction under paragraph (h)(2) of this section over the portion of any excess business interest expense allocated to the transferor under paragraph (f)(2) of this section which has previously been treated under paragraph (g) of this

section as business interest expense paid or accrued by the transferor, multiplied by the ratio of the fair market value of the transferred interest to the total fair market value of the transferor's partnership interest immediately prior to the disposition. Therefore, the adjusted basis of the transferred interest is not increased immediately before the disposition by any allocation of excess business interest expense from the partnership that did not reduce the transferor's adjusted basis in its partnership interest pursuant to paragraph (h) of this section prior to the disposition, or by any excess business interest expense that was treated under paragraph (g) of this section as business interest expense paid or accrued by the transferor prior to the disposition. If the transferor disposes of all of its partnership interest, no deduction under section 163(j) is allowed to the transferor or transferee under chapter 1 of subtitle A of the Code for any excess business interest expense or negative section 163(j) expense. If the transferor disposes of a portion of its partnership interest, no deduction under section 163(j) is allowed to the transferor or transferee under chapter 1 of subtitle A of the Code for the amount of excess business interest expense proportionate to the transferred interest. The amount of excess business interest expense proportionate to the partnership interest retained by the transferor shall remain as excess business interest expense of the transferor until such time as such excess business interest expense is treated as business interest expense paid or accrued by the transferor pursuant to paragraph (g) of this section. Further, if the transferor disposes of a portion of its partnership interest, any negative section 163(j) expense shall remain negative section 163(j) expense of the transferor partner until such negative section 163(j) expense is no longer suspended under section 704(d). For purposes of this paragraph, a disposition includes a distribution of money or other property by the partnership to a partner in complete liquidation of its interest in the partnership. Further, solely for purposes of this section, each partner is considered to have disposed of its partnership interest if the partnership terminates under section 708(b)(1). See *Example 9* and *Example 10* in paragraphs (o)(9) and (o)(10) of this section, respectively.

(i)–(j) [Reserved]

(k) *Investment items and certain other items.* Any item of a partnership's income, gain, deduction, or loss that is investment interest income or expense pursuant to § 1.163–8T, and any other tax item of a partnership that is neither properly allocable to a trade or business of the partnership nor described in section 163(d), is allocated to each partner in accordance with section 704(b) and the regulations under section 704 of the Code, and the effect of such allocation for purposes of section 163 is determined at the partner-level. See § 1.163(j)–4(b)(3), section 163(d), and § 1.163–8T.

(l) *S corporations*—(1) *In general—(i) Corporate level limitation.* In the case of any S corporation, the section 163(j) limitation is applied at the S corporation level, and any deduction allowed for business interest expense is taken into account in determining the nonseparately stated taxable income or loss of the S corporation. An S corporation determines its section 163(j) limitation in the same manner as set forth in § 1.163(j)–2(b). Allocations of excess taxable income and excess business interest income are made in accordance with the shareholders' pro rata interests in the S corporation pursuant to section 1366(a)(1) after determining the S corporation's section 163(j) limitation pursuant to § 1.163(j)–2(b). See *Example 22* and *Example 23* in paragraphs (o)(22) and (23) of this section, respectively.

(ii) *Short taxable periods.* For rules on applying the section 163(j) limitation where an S corporation has a two short taxable periods or where its taxable year consists of two separate taxable years see §§ 1.1362–3(c), 1.1368–1(g), and 1.1377–1(b).

(2) *Character of deductible business interest expense.* If an S corporation has deductible business interest expense, such deductible business interest expense is not subject to any additional application of section 163(j) at the shareholder-level because such deductible business interest expense is taken into account in determining the nonseparately stated taxable income or loss of the S corporation. However, for all other purposes of the Code, deductible business interest expense retains its character as business interest expense at the shareholder-level. For example, for purposes of section 469, such deductible business interest expense retains its character as either passive or non-passive in the hands of the shareholder. Additionally, for purposes of section 469, deductible business interest expense from an S corporation remains interest derived from a trade or business in the hands of a shareholder even if the shareholder does not materially participate in the S corporation's trade or business activity. For additional rules regarding the interaction between sections 465, 469, and 163(j), see § 1.163(j)–3.

(3) *Adjusted taxable income of an S corporation.* The ATI of an S corporation generally is determined in accordance with § 1.163(j)–1(b)(1). For purposes of computing the S corporation's ATI, the tentative taxable income of the S corporation is determined under section 1363(b) and includes—

(i) Any item described in section 1363(b)(1); and

(ii) Any item described in § 1.163(j)–1(b)(1), to the extent such item is consistent with subchapter S of the Code.

(4) *Adjusted taxable income and business interest income of S corporation shareholders*—(i) *Adjusted taxable income of S corporation shareholders.* The ATI of an S corporation shareholder is determined in accordance with § 1.163(j)–1(b)(1) without regard to such shareholder's distributive share of any items of income, gain, deduction, or loss of such S corporation, except as provided in paragraph (m), and is increased by such shareholder's distributive share of such S corporation's excess taxable income.

(ii) *Disposition of S corporation stock.* If a shareholder of an S corporation recognizes gain or loss upon the disposition of stock of the S corporation, and the corporation the stock of which is being disposed of only owns non-excepted trade or business assets, the gain or loss on the disposition of the stock is included in the shareholder's ATI. See § 1.163(j)–10(b)(4)(ii) for dispositions of stock of S corporations that own—

(A) Non-excepted assets and excepted assets; or

(B) Investment assets; or

(C) Both.

(iii) *Double counting of business interest income and floor plan financing interest expense prohibited.* For purposes of calculating an S corporation shareholder's section 163(j) limitation, the shareholder does not include—

(A) Business interest income from an S corporation that is subject to section 163(j), except to the extent the shareholder is allocated excess business interest income from that S corporation pursuant to paragraph (l)(1) of this section; and

(B) The shareholder's share of the S corporation's floor plan financing interest expense, because such floor plan financing interest expense already has been taken into account by the S corporation in determining its nonseparately stated taxable income or loss for purposes of section 163(j).

(5) *Carryforwards.* The amount of any business interest expense not allowed as a deduction for any taxable year by reason of the limitation contained in § 1.163(j)–2(b) is carried forward in the succeeding taxable year as a disallowed business interest expense carryforward under the rules set forth in § 1.163(j)–2(c) (whether to an S corporation taxable year or a C corporation taxable year). For purposes of applying section 163(j), S corporations are subject to the same ordering rules as a C corporation that is not a member of a consolidated group. See § 1.163(j)–5(b)(2).

(6) *Basis adjustments and disallowed business interest expense carryforwards.* An S corporation shareholder's adjusted basis in its S corporation stock is reduced, but not below zero, when a disallowed business interest expense carryforward becomes deductible under section 163(j).

(7) *Accumulated adjustment accounts.* The accumulated adjustment account of an S corporation is adjusted to take into account business interest expense in the year in which the S corporation treats such business interest expense as deductible under the section 163(j) limitation. See section 1368(e)(1).

(8) *Termination of qualified subchapter S subsidiary election.* If a corporation's qualified subchapter S subsidiary election terminates and any disallowed business interest expense carryforward is attributable to the activities of the qualified subchapter S subsidiary at the time of termination, such disallowed business interest expense carryforward remains with the parent S corporation, and no portion of these items is allocable to the former qualified subchapter S subsidiary.

(9) *Investment items.* Any item of an S corporation's income, gain, deduction, or loss that is investment interest income or expense pursuant to § 1.163–8T is allocated to each shareholder in accordance with the shareholders' pro rata interests in the S corporation pursuant to section 1366(a)(1). See section 163(d) and § 1.163–8T.

(10) *Application of section 382.* In the event of an ownership change, within the meaning of section 382(g), the S corporation's business interest expense is subject to section 382. Therefore, the allocation of the S corporation's business interest expense between the pre-change period (as defined in § 1.382–6(g)(2)) and the post-change period (as defined in § 1.382–6(g)(3)), and the determination of the amount that is deducted and carried forward, is determined pursuant to § 1.382–6. If the date of the ownership change is also the date of a qualifying disposition (as defined in § 1.1368–1(g)(2)) or the date for a termination of shareholder interest (as defined in § 1.1377–1(b)(4)), then—

(i) The rules of this paragraph govern the S corporation's business interest expense;

(ii) The S corporation must make an election under § 1.382–6(b) with respect to such date if it also makes an election under § 1.1368–1(g)(2) or a shareholder termination election to apply normal tax accounting rules, as applicable, with respect to such date; and

(iii) The S corporation may not make an election under § 1.382–6(b) with respect to such date if it does not make an election under § 1.1368–1(g)(2) or a termination election under § 1.1377–1(b)(1), as applicable, with respect to such date.

(m) *Partnerships and S corporations not subject to section 163(j)*—(1) *Exempt partnerships and S corporations.* If the small business exemption in § 1.163(j)–2(d) applies to a partnership or an S corporation in a taxable year (exempt entity), the general rule in § 1.163(j)–2 and this section does not apply to limit the deduction for business interest expense of the exempt entity in that taxable year. Additionally, if a partner or S corporation shareholder is allocated business interest expense from an exempt entity, such business interest expense is not subject to the section 163(j) limitation at the partner's or S corporation shareholder's level. However, see paragraph (h)(1) of this section. Further, a partner or S corporation shareholder of an exempt entity includes its share of non-excepted trade or business items of income, gain, loss, and deduction (including business interest expense and business interest income) of such exempt entity when calculating its ATI. However, if a partner's or S corporation shareholder's allocations of non-excepted trade or business items of loss and deduction from an exempt entity exceed its allocations of non-excepted trade or business items of income and gain from such exempt entity (net loss allocation), then such net loss allocation will not reduce a partner's or S corporation shareholder's ATI. See *Example 11* and *Example 12* in paragraphs (o)(11) and (12) of this section, respectively.

(2) *Partnerships and S corporations engaged in excepted trades or businesses.* To the extent a partnership or an S corporation is engaged in an excepted trade or business, the general rule in § 1.163(j)–2 and this section does not apply to limit the deduction for business interest expense that is allocable to such excepted trade or business. If a partner or S corporation shareholder is allocated any section 163(j) item that is allocable to an excepted trade or business of the partnership or S corporation (excepted 163(j) items), such excepted 163(j) items are excluded from the partner's or shareholder's section 163(j) deduction calculation. See § 1.163(j)–10(c) (regarding the allocation of items between excepted and non-excepted trades or businesses). See also *Example 13* in paragraph (o)(13) of this section.

(3) *Treatment of excess business interest expense from partnerships that are exempt entities in a succeeding taxable year.* If a partner is allocated excess business interest expense from a partnership and, in a succeeding taxable year, such partnership is an exempt entity, then the partner shall treat any of its excess business interest expense that was previously allocated from such partnership as business interest expense paid or accrued by the partner in such succeeding taxable year, which is potentially subject to limitation at the partner level under section 163(j). However, if a partner is allocated excess business interest expense from a partnership and, in a succeeding taxable year, such partnership engages in excepted trades or businesses, then the partner shall not treat any of its excess business interest expense that was previously allocated from such partnership as business interest expense paid or accrued by the partner in such succeeding taxable year by reason of the partnership engaging in excepted trades or businesses. See *Example 14* through *Example 16* in paragraphs (o)(14) through (o)(16) of this section, respectively. For rules regarding the treatment of excess business interest expense from a partnership that terminates under section 708(b)(1), see paragraph (h)(3) of this section.

(4) *S corporations with disallowed business interest expense carryforwards prior to becoming exempt entities.* If an S corporation has a disallowed business interest expense carryforward for a taxable year and, in a succeeding taxable year, such S corporation is an exempt entity, then such disallowed business interest expense carryforward—

(i) Continues to be carried forward at the S corporation level;

(ii) Is no longer subject to the section 163(j) limitation; and

(iii) Is taken into account in determining the nonseparately stated taxable income or loss of the S corporation.

(n) [Reserved]

(o) *Examples.* The examples in this paragraph illustrate the provisions of section 163(j) as applied to partnerships and subchapter S corporations. For purposes of these examples, unless stated otherwise, each partnership and S corporation is subject to the provisions of section 163(j), is only engaged in non-excepted trades or businesses, was created or organized in the United States, and uses the calendar year for its annual accounting period. Unless stated otherwise, all partners and shareholders are subject to the provisions of section 163(j), are not subject to a limitation under section 704(d) or 1366(d), have no tax items other than those listed in the example, are U.S. citizens, and use the calendar year for their annual accounting period. The phrase ''section 163(j) limit'' shall equal the maximum potential deduction allowed under section 163(j)(1). Unless stated otherwise, business interest expense means business interest expense that is not floor plan financing interest expense. With respect to partnerships, all allocations are in accordance with section 704(b) and the regulations in this part under section 704 of the Code.

(1) *Example 1*—(i) *Facts.* X and Y are equal partners in partnership PRS. In Year 1, PRS has $100 of ATI and $40 of business interest expense. PRS allocates the items comprising its $100 of ATI $50 to X and $50 to Y. PRS allocates its $40 of business interest expense $20 to X and $20 to Y. X has $100 of ATI and $20 of business interest expense from its sole proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 1, PRS's section 163(j) limit is 30 percent of its ATI, or $30 ($100 × 30 percent). Thus, PRS has $30 of deductible business interest expense and $10 of excess business interest expense. Such $30 of deductible business interest expense is includable in PRS's nonseparately stated income or loss, and is not subject to further limitation under section 163(j) at the partners' level.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X and Y are each allocated $15 of deductible business interest expense and $5 of excess business interest expense. At the end of Year 1, X and Y each have $5 of excess business interest expense from PRS, which is not treated as paid or accrued by the partner until such partner is allocated excess taxable income or excess business interest income from PRS in a succeeding taxable year. Pursuant to § 1.163(j)–6(e)(1), X and Y, in computing their limit under section 163(j), do not increase any of their section 163(j) items by any of PRS's section 163(j) items. X and Y each increase their outside basis in PRS by $30 ($50 − $20).

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $100 of ATI and $20 of business interest expense from its sole proprietorship. X's section 163(j) limit is $30 ($100 × 30 percent). Thus, X's $20 of business interest expense is deductible business interest expense. Y, in computing its limit under section 163(j), has $20 of business interest expense from its sole proprietorship. Y's section 163(j) limit is $0 ($0 × 30 percent). Thus, Y's $20 of business interest expense is not allowed as a deduction and is treated as business interest expense paid or accrued by Y in Year 2.

(2) *Example 2*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (o)(1)(i) of this section. In Year 2, PRS has $200 of ATI, $0 of business interest income, and $30 of business interest expense. PRS allocates the items comprising its $200 of ATI $100 to X and $100 to Y. PRS allocates its $30 of business interest expense $15 to X and $15 to Y. X has $100 of ATI and $20 of business interest expense from its sole proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 2, PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $60 ($200 × 30 percent). Thus, PRS has $100 of excess taxable income, $30 of deductible business interest expense, and $0 of excess business interest expense. Such $30 of deductible business interest expense is includable in PRS's nonseparately stated income or loss, and is not subject to further limitation under section 163(j) at the partners' level.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X and Y are each allocated $50 of excess taxable income, $15 of deductible business interest expense, and $0 of excess business interest expense. As a result, X and Y each increase their ATI by $50. Because X and Y are each allocated $50 of excess taxable income from PRS, and excess business interest expense from a partnership is treated as paid or accrued by a partner to the extent excess taxable income and excess business interest income are allocated from such partnership to a partner, X and Y each treat $5 of excess business interest expense (the carryforward from Year 1) as paid or accrued in Year 2. X and Y each increase their outside basis in PRS by $85 ($100 − $15).

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $150 of ATI ($100 from its sole proprietorship, plus $50 excess taxable income) and $25 of business interest expense ($20 from its sole proprietorship, plus $5 excess business interest expense treated as paid or accrued in Year 2). X's section 163(j) limit is $45 ($150 × 30 percent). Thus, X's $25 of business interest expense is deductible business interest expense. At the end of Year 2, X has $0 of excess business interest expense from PRS ($5 from Year 1, less $5 treated as paid or accrued in Year 2). Y, in computing its limit under section 163(j), has $50 of ATI ($0 from its sole proprietorship, plus $50 excess taxable income) and $45 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from Year 1, plus $5 excess business interest expense treated as paid or accrued in Year 2). Y's section 163(j) limit is $15 ($50 × 30 percent). Thus, $15 of Y's business interest expense is deductible business interest expense. The $30 of Y's business interest expense not allowed as a deduction ($45 business interest expense, less $15 section 163(j) limit) is treated as business interest expense paid or accrued by Y in Year 3. At the end of Year 2, Y has $0 of excess business interest expense from PRS ($5 from Year 1, less $5 treated as paid or accrued in Year 2).

(3) *Example 3*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (o)(1)(i) of this section. In Year 2, PRS has $0 of ATI, $60 of business interest income, and $40 of business interest expense. PRS allocates its $60 of business interest income $30 to X and $30 to Y. PRS allocates its $40 of business interest expense $20 to X and $20 to Y. X has $100 of ATI and $20 of business interest expense from its sole proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 2, PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $60 (($0 × 30 percent) + $60). Thus, PRS has $20 of excess business interest income, $0 of excess taxable income, $40 of deductible business interest expense, and $0 of excess business interest expense. Such $40 of deductible business interest expense is includable in PRS's nonseparately stated income or loss, and is not subject to further limitation under section 163(j) at the partners' level.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X and Y are each allocated $10 of excess business interest income, and $20 of deductible business interest expense. As a result, X and Y each increase their business interest income by $10. Because X and Y are each allocated $10 of excess business interest income from PRS, and excess business interest expense from a partnership is treated as paid or accrued by a partner to the extent excess taxable income and excess business interest income are allocated from such partnership to a partner, X and Y each treat $5 of excess business interest expense (the carryforward from Year 1) as paid or accrued in Year 2. X and Y each increase their outside basis in PRS by $10 ($30 − $20).

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $100 of ATI (from its sole proprietorship), $10 of business interest income (from the allocation of $10 of excess business interest income from PRS), and $25 of business interest expense ($20 from its sole proprietorship, plus $5 excess business interest expense treated as paid or accrued in Year 2). X's section 163(j) limit is $40 (($100 × 30 percent) + $10). Thus, X's $25 of business interest expense is deductible business interest expense. At the end of Year 2, X has $0 of excess business interest expense from PRS ($5 from Year 1, less $5 treated as paid or accrued in Year 2). Y, in computing its limit under section 163(j), has $0 of ATI (from its sole proprietorship), $10 of business interest income, and $45 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from Year 1, plus $5 excess business interest expense treated as paid or accrued in Year 2). Y's section 163(j) limit is $10 (($0 × 30 percent) + $10). Thus, $10 of Y's business interest expense is deductible business interest expense. The $35 of Y's business interest expense not allowed as a deduction ($45 business interest expense, less $10 section 163(j) limit) is treated as business interest expense paid or accrued by Y in Year 3. At the end of Year 2, Y has $0 of excess business interest expense from PRS ($5 from Year 1, less $5 treated as paid or accrued in Year 2).

(4) *Example 4*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (o)(1)(i) of this section. In Year 2, PRS has $100 of ATI, $60 of business interest income, and $40 of business interest expense. PRS allocates the items comprising its $100 of ATI $50 to X and $50 to Y. PRS allocates its $60 of business interest income $30 to X and $30 to Y. PRS allocates its $40 of business interest expense $20 to X and $20 to Y. X has $100 of ATI and $20 of business interest expense from its sole proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 2, PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $90 (($100 × 30 percent)) + $60). Thus, PRS has $20 of excess business interest income, $100 of excess taxable income, $40 of deductible business interest expense, and $0 of excess business interest expense. Such $40 of deductible business interest expense is includable in PRS's nonseparately stated income or loss, and is not subject to further limitation under section 163(j) at the partners' level.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X and Y are each allocated $10 of excess business interest income, $50 of excess taxable income, and $20 of deductible business interest expense. As a result, X and Y each increase their business interest income by $10 and ATI by $50. Because X and Y are each allocated $10 of excess business interest income and $50 of excess taxable income from PRS, and excess business interest expense from a partnership is treated as paid or accrued by a partner to the extent excess taxable income and excess business interest income are allocated from such partnership to a partner, X and Y each treat $5 of excess business interest expense (the carryforward from Year 1) as paid or accrued in Year 2. X and Y each increase their outside basis in PRS by $60 ($80 − $20).

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $150 of ATI ($100 from its sole proprietorship, plus $50 excess taxable income), $10 of business interest income, and $25 of business interest expense ($20 from its sole proprietorship, plus $5 excess business interest expense treated as paid or accrued in Year 2). X's section 163(j) limit is $55 (($150 × 30 percent) + $10). Thus, $25 of X's business interest expense is deductible business interest expense. At the end of Year 2, X has $0 of excess business interest expense from PRS ($5 from Year 1, less $5 treated as paid or accrued in Year 2). Y, in computing its limit under section 163(j), has $50 of ATI ($0 from its sole proprietorship, plus $50 excess taxable income), $10 of business interest income, and $45 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from Year 1, plus $5 excess business interest expense treated as paid or accrued in Year 2). Y's section 163(j) limit is $25 (($50 × 30 percent) + $10). Thus, $25 of Y's business interest expense is deductible business interest expense. Y's $20 of business interest expense not allowed as a deduction ($45 business interest expense, less $25 section 163(j) limit) is treated as business interest expense paid or accrued by Y in Year 3. At the end of Year 2, Y has $0 of excess business interest expense from PRS ($5 from Year 1, less $5 treated as paid or accrued in Year 2).

(5) *Example 5*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (o)(1)(i) of this section. In Year 2, PRS has $100 of ATI, $11.20 of business interest income, and $40 of business interest expense. PRS allocates the items comprising its $100 of ATI $50 to X and $50 to Y. PRS allocates its $11.20 of business interest income $5.60 to X and $5.60 to Y. PRS allocates its $40 of business interest expense $20 to X and $20 to Y. X has $100 of ATI and $20 of business interest expense from its sole proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 2, PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $41.20 (($100 × 30 percent) + $11.20). Thus, PRS has $0 of excess business interest income, $4 of excess taxable income, and $40 of deductible business interest expense. Such $40 of deductible business interest expense is includable in PRS's nonseparately stated income or loss, and is not subject to further limitation under section 163(j) at the partners' level.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X and Y are each allocated $2 of excess taxable income, $20 of deductible business interest expense, and $0 of excess business interest expense. As a result, X and Y each increase their ATI by $2. Because X and Y are each allocated $2 of excess taxable income from PRS, and excess business interest expense from a partnership is treated as paid or accrued by a partner to the extent excess taxable income and excess business interest income are allocated from such partnership to a partner, X and Y each treat $2 of excess business interest expense (a portion of the carryforward from Year 1) as paid or accrued in Year 2. X and Y each increase their outside basis in PRS by $35.60 ($55.60 − $20).

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $102 of ATI ($100 from its sole proprietorship, plus $2 excess taxable income), $0 of business interest income, and $22 of business interest expense ($20 from its sole proprietorship, plus $2 excess business interest expense treated as paid or accrued). X's section 163(j) limit is $30.60 ($102 × 30 percent). Thus, X's $22 of business interest expense is deductible business interest expense. At the end of Year 2, X has $3 of excess business interest expense from PRS ($5 from Year 1, less $2 treated as paid or accrued in Year 2).

Y, in computing its limit under section 163(j), has $2 of ATI ($0 from its sole proprietorship, plus $2 excess taxable income), $0 of business interest income, and $42 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from Year 1, plus $2 excess business interest expense treated as paid or accrued in Year 2). Y's section 163(j) limit is $0.60 ($2 × 30 percent). Thus, $0.60 of Y's business interest expense is deductible business interest expense. Y's $41.40 of business interest expense not allowed as a deduction ($42 business interest expense, less $0.60 section 163(j) limit) is treated as business interest expense paid or accrued by Y in Year 3. At the end of Year 2, Y has $3 of excess business interest expense from PRS ($5 from Year 1, less $2 treated as paid or accrued in Year 2).

(6) *Example 6*—(i) *Facts.* In Year 1, X, Y, and Z formed partnership PRS. Upon formation, X and Y each contributed $100, and Z contributed non-excepted and non-depreciable trade or business property with a basis of $0 and fair market value of $100 (Blackacre). PRS allocates all items pro rata between its partners. Immediately after the formation of PRS, Z sold all of its interest in PRS to A for $100 (assume the interest sale is respected for U.S. Federal income tax purposes). In connection with the interest transfer, PRS made a valid election under section 754. Therefore, after the interest sale, A had a $100 positive section 743(b) adjustment in Blackacre. In Year 1, PRS had $0 of ATI, $15 of business interest expense, and $0 of business interest income. Pursuant to § 1.163(j)–6(f)(2), PRS allocated each of the partners $5 of excess business interest expense. In Year 2, PRS sells Blackacre for $100 which generated $100 of ATI. The sale of Blackacre was PRS's only item of income in Year 2. In accordance with section 704(c), PRS allocates all $100 of gain resulting from the sale of Blackacre to A. Additionally, PRS has $15 of business interest expense, all of which it allocates to X. A has $50 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 2, PRS's section 163(j) limit is 30 percent of its ATI, or $30 ($100 × 30 percent). Thus, PRS has $15 of deductible business interest expense and $50 of excess taxable income. Such $15 of deductible business interest expense is includable in PRS's nonseparately stated income or loss, and is not subject to further limitation under section 163(j) at X's level.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X is allocated $15 of deductible business interest expense and X's outside basis in PRS is reduced by $15. A is allocated $50 of excess taxable income and, as a result, A increases its ATI by $50. Because A is allocated $50 of excess taxable income, and excess business interest expense from a partnership is treated as paid or accrued by a partner to the extent excess taxable income and excess business interest income are allocated from such partnership to a partner, A treats $5 of excess business interest expense (the carryforward from Year 1) as paid or accrued in Year 2. PRS's $100 of gain allocated to A in Year 2 is fully reduced by A's $100 section 743(b) adjustment. Therefore, at the end of Year 2, there is no change to A's outside basis in PRS.

(iv) *Partner-level.* A, in computing its limit under section 163(j), has $0 of ATI ($50 from its sole proprietorship, plus $50 excess taxable income, less $100 ATI reduction as a result of A's section 743(b) adjustment under § 1.163(j)–6(e)(2)) and $25 of business interest expense ($20 from its sole proprietorship, plus $5 excess business interest expense treated as paid or accrued in Year 2). A's section 163(j) limit is $0 ($0 × 30 percent). Thus, all $25 of A's business interest expense is not allowed as a deduction and is treated as business interest expense paid or accrued by A in Year 3.

(7) *Example 7*—(i) *Facts.* X and Y are equal partners in partnership PRS. At the beginning of Year 1, X and Y each have an outside basis in PRS of $5. In Year 1, PRS has $0 of ATI, $20 of business interest income, and $40 of business interest expense. PRS allocates its $20 of business interest income $10 to X and $10 to Y. PRS allocates $40 of business interest expense $20 to X and $20 to Y. X has $100 of ATI and $20 of business interest expense from its sole proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 1, PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $20 (($0 × 30 percent) + $20). Thus, PRS has $0 of excess business interest income, $0 of excess taxable income, $20 of deductible business interest expense, and $20 of excess business interest expense. Such $20 of deductible business interest expense is includable in nonseparately stated income or loss of PRS, and not subject to further limitation under section 163(j) by the partners.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X and Y are each allocated $10 of deductible business interest expense and $10 of excess business interest expense. After adjusting each partner's respective basis for business interest income under section 705(a)(1)(A), pursuant to § 1.163(j)–6(h)(1), X and Y each take their $10 of deductible business interest expense into account when reducing their outside basis in PRS before taking the $10 of excess business interest expense into account. Following each partner's reduction in outside basis due to the $10 of deductible business interest expense, each partner has $5 of outside basis remaining in PRS. Pursuant to § 1.163(j)–6(h)(2), each partner has $5 of excess business interest expense and $5 of negative section 163(j) expense. In sum, at the end of Year 1, X and Y each have $5 of excess business interest expense from PRS which reduces each partner's outside basis to $0 (and is not treated as paid or accrued by the partners until such partner is allocated excess taxable income or excess business interest income from PRS in a succeeding taxable year), and $5 of negative section 163(j) expense (which is suspended under section 704(d) and not treated as excess business interest expense of the partners until such time as the negative section 163(j) expense is no longer subject to a limitation under section 704(d)).

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $100 of ATI (from its sole proprietorship) and $20 of business interest expense (from its sole proprietorship). X's section 163(j) limit is $30 ($100 × 30 percent). Thus, $20 of X's business interest expense is deductible business interest expense. Y, in computing its limit under section 163(j), has $20 of business interest expense (from its sole proprietorship). Y's section 163(j) limit is $0 ($0 × 30 percent). Thus, $20 of Y's business interest expense is not allowed as a deduction in Year 1, and is treated as business interest expense paid or accrued by Y in Year 2.

(8) *Example 8*—(i) *Facts.* The facts are the same as in *Example 7* in paragraph (o)(7)(i) of this section. In Year 2, PRS has $20 of gross income that is taken into account in determining PRS's ATI (in other words, properly allocable to a trade or business), $30 of gross deductions from an investment activity, and $0 of business interest expense. PRS allocates the items comprising its $20 of ATI $10 to X and $10 to Y. PRS allocates the items comprising its $30 of gross deductions $15 to X and $15 to Y. X has $100 of ATI and $20 of business interest expense from its sole

proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 2, PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $6 ($20 × 30 percent). Because PRS has no business interest expense, all $20 of its ATI is excess taxable income.

(iii) *Partner-level allocations.* Pursuant to § 1.163(j)–6(f)(2), X and Y are each allocated $10 of excess taxable income. Because X and Y are each allocated $10 of excess taxable income from PRS, X and Y each increase their ATI by $10. Pursuant to § 1.704–(1)(d)(2), each partner's limitation on losses under section 704(d) must be allocated to its distributive share of each such loss. Thus, each partner reduces its adjusted basis of $10 (attributable to the allocation of items comprising PRS's ATI in Year 2) by $7.50 of gross deductions from Year 2 ($10 × ($15 of total gross deductions from Year 2/$20 of total losses disallowed)), and $2.50 of excess business interest expense that was carried over as negative section 163(j) expense from Year 1 ($10 × ($5 of negative section 163(j) expense treated as excess business interest expense solely for the purposes of section 704(d)/$20 of total losses disallowed)). Following the application of section 704(d), each partner has $7.50 of excess business interest expense from PRS ($5 excess business interest expense from Year 1, plus $2.50 of excess business interest expense that was formerly negative section 163(j) expense carried over from Year 1). Excess business interest expense from a partnership is treated as paid or accrued by a partner to the extent excess taxable income and excess business interest income are allocated from such partnership to the partner. As a result, X and Y each treat $7.50 of excess business interest expense as paid or accrued in Year 2.

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $110 of ATI ($100 from its sole proprietorship, plus $10 excess taxable income) and $27.50 of business interest expense ($20 from its sole proprietorship, plus $7.50 excess business interest expense treated as paid or accrued in Year 2). X's section 163(j) limit is $33 ($110 × 30 percent). Thus, $27.50 of X's business interest expense is deductible business interest expense. At the end of Year 2, X has $0 of excess business interest expense from PRS ($5 from Year 1, plus $2.50 treated as excess business interest expense in Year 2, less $7.50 treated as paid or accrued in Year 2), and $2.50 of negative section 163(j) expense from PRS. Y, in computing its limit under section 163(j), has $10 of ATI ($0 from its sole proprietorship, plus $10 excess taxable income) and $47.50 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from Year 1, plus $7.50 excess business interest expense treated as paid or accrued in Year 2). Y's section 163(j) limit is $3 ($10 × 30 percent). Thus, $3 of Y's business interest expense is deductible business interest expense. The $44.50 of Y's business interest expense not allowed as a deduction ($47.50 business interest expense, less $3 section 163(j) limit) is treated as business interest expense paid or accrued by Y in Year 3. At the end of Year 2, Y has $0 of excess business interest expense from PRS ($5 from Year 1, plus $2.50 treated as excess business interest expense in Year 2, less $7.50 treated as paid or accrued in Year 2), and $2.50 of negative section 163(j) expense from PRS.

(9) *Example 9*—(i) *Facts.* X and Y are equal partners in partnership PRS, and are not members of a consolidated group. At the beginning of Year 1, X and Y each have $120 of outside basis in PRS. Neither X nor Y's share of partnership liabilities exceeds the adjusted basis of its entire interest. In Year 1, X is allocated $20 of excess business interest expense, which reduces its outside basis from $120 to $100. In Year 2, X sells 80 percent of its interest in PRS to Z for $160. Immediately prior to the sale, X's entire PRS interest had a fair market value of $200 and the transferred portion of the interest had a fair market value of $160.

(ii) *Basis adjustment.* Immediately before the sale to Z, X increases its basis in the portion of the interest sold by 80 percent of the amount of the excess of the amount of the basis reduction under paragraph (h)(2) of this section ($20) over the portion of any excess business interest expense allocated the partner under paragraph (f)(2) of this section that has previously been treated under paragraph (g) of this section as business interest expense paid or accrued by X ($0). Therefore, X's basis in the portion of its interest sold is $96 (($100 × 80%) + ($20 × 80%)), and X's gain is $64 ($160 − $96). Following the sale, X has $20 of outside basis in its remaining partnership interest and $4 of excess business interest expense.

(10) *Example 10*—(i) *Facts.* X and Y are equal partners in partnership PRS, and are not members of a consolidated group. At the beginning of Year 1, X and Y each have an outside basis in PRS of $10. Neither X nor Y's share of partnership liabilities exceeds the adjusted basis of its entire interest. In Year 1, X is allocated $8 of excess business interest expense and $12 of loss from PRS. As a result, X has $4 of excess business interest expense, $4 of negative section 163(j) expense, $6 of allowable loss, $6 of loss suspended under section 704(d), and $0 of outside basis in PRS at the end of Year 1. In Year 2, X sells 50 percent of its interest in PRS to Z for $20. Immediately prior to the sale, X's entire partnership interest had a fair market value of $40 and the transferred portion of the interest had a fair market value of $20.

(ii) *Basis adjustment.* Immediately before the sale to Z, X increases its basis in the portion of the interest sold by 50 percent of the amount of the excess of the amount of the basis reduction under paragraph (h)(2) of this section ($4) over the portion of any excess business interest expense allocated the partner under paragraph (f)(2) of this section that has previously been treated under paragraph (g) of this section as business interest expense paid or accrued by X ($0). Therefore, X's basis in the portion of its interest sold is $2 (($0 × 50%) + $2), and X's gain is $18 ($20 − $2). Following the sale, X has $0 of outside basis in its remaining partnership interest, $2 of excess business interest expense, $4 of negative section 163(j) expense, and $6 of loss suspended under section 704(d).

(11) *Example 11*—(i) *Facts.* X (a corporation), Y (an individual), and Z (an individual) are equal partners in partnership PRS. X, Y, and Z are subject to section 163(j). PRS is not subject to section 163(j) under section 163(j)(3). In 2021, PRS has $150 of trade or business income (not taking into account business interest income or business interest expense), $30 of business interest income, and $45 of business interest expense. PRS also has $75 of investment income and $60 of investment interest expense. PRS allocates its items of income, gain, loss, and deduction equally among its partners. X, Y, and Z each have $10 of business interest expense from their respective businesses.

(ii) *Partnership-level.* PRS is not subject to section 163(j) by reason of section 163(j)(3). As a result, none of PRS's $45 of business interest expense is subject to the section 163(j) limitation.

(iii) *Partner-level allocations.* Because PRS is not subject to section 163(j) by reason of section 163(j)(3), PRS's $45 of business interest expense does not retain its character as business interest expense for purposes of section 163(j). As a result, such business interest expense is not subject to the section 163(j) limitation at the level of either the partnership or partner. Additionally, pursuant to § 1.163(j)–6(m)(1), each partner includes its share of non-excepted trade or business items of income, gain, loss, and deduction (including business interest expense and business interest income) of PRS when calculating its ATI. As a result, each partner increases its ATI by $45 (one third of $150 + $30 − $45). Also, X increases its ATI by an additional $25 because its items of investment income and loss from PRS are recharacterized as non-excepted trade or business income and loss at its level pursuant to §§ 1.163(j)–4(b)(3)(i) and 1.163(j)–10(b)(6). Further, X increases its business interest expense by its $20 allocation of investment interest expense from PRS pursuant to §§ 1.163(j)–4(b)(3)(i) and 1.163(j)–10(b)(6).

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $70 of ATI and $30 of business interest expense. X's section 163(j) limit is $21 ($70 × 30 percent). Thus, X has $21 of deductible business interest expense. X's $9 of business interest expense not allowed as a deduction is treated as business interest expense paid or accrued by X in 2020. Y and Z, in computing their respective limits under section 163(j), each have $45 of ATI and $10 of business interest expense. Y and Z each have a section 163(j) limit of $13.50 ($45 − 30 percent). Thus, Y and Z each have $10 of deductible business interest expense.

(12) *Example 12*—(i) *Facts.* The facts are the same as in *Example 11* in paragraph (o)(11)(i) of this section, except PRS has $200 of depreciation deductions in addition to its other items of income, gain, loss, and deduction.

(ii) *Partnership-level.* Same analysis as *Example 11* in paragraph (o)(11)(ii) of this section.

(iii) *Partner-level allocations.* Because PRS is not subject to section 163(j) by reason of section 163(j)(3), PRS's $45 of business interest expense does not retain its character as business interest expense for purposes of section 163(j). As a result, such business interest expense is not subject to the section 163(j) limitation at the level of either the partnership or partner. Additionally, pursuant to § 1.163(j)–6(m)(1), each partner includes its share of non-excepted trade or business items of income, gain, loss, and deduction (including business interest expense and business interest income) of PRS when calculating its ATI; however, a net loss allocation of trade or business items from an exempt entity does not reduce a partner's ATI. Because each of the partners has a net loss allocation of trade or business items from PRS, none of the partners adjust their ATI for the trade or business items of PRS. X, the corporate partner, increases its ATI by $25 because its items of investment income and loss from PRS are recharacterized as trade or business income and loss at its level pursuant to §§ 1.163(j)–4(b)(3)(i) and 1.163(j)–10(b)(6). Further, X increases its business interest expense by its $20 allocation of investment interest expense from PRS pursuant to §§ 1.163(j)–4(b)(3)(i) and 1.163(j)–10(b)(6).

(iv) *Partner-level computations.* In computing its limit under section 163(j), each partner has $0 of ATI and $10 of business interest expense. Each partner's section 163(j) limit is $0 ($0 × 30 percent). Thus, each partner's $10 of business interest expense is not allowed as a deduction and is treated as business interest expense paid or accrued by the partner in 2020. X, in computing its limit under section 163(j), has $25 of ATI and $30 of business interest expense. X's section 163(j) limit is $7.50 ($25 × 30 percent). Thus, X has $7.50 of deductible business interest expense. X's $22.50 of business interest expense not allowed as a deduction is treated as business interest expense paid or accrued by X in 2020. Y and Z, in computing their respective limits under section 163(j), each have $0 of ATI and $10 of business interest expense. Thus, Y and Z each have $10 of business interest expense not allowed as a deduction that is treated as business interest expense paid or accrued in 2020.

(13) *Example 13*—(i) *Facts.* X, Y, and Z are equal partners in partnership PRS. X, Y, and Z are each individuals subject to section 163(j). PRS is not subject to section 163(j) under section 163(j)(3). PRS has one excepted and one non-excepted trade or business. In Year 1, PRS has $200 of income and $10 of business interest expense from its excepted trade or business, and $60 of business interest income and $30 of business interest expense from its non-excepted trade or business. PRS allocates its items of income, gain, loss, and deduction equally among its partners. X, Y, and Z each have $10 of business interest expense from their respective businesses.

(ii) *Partnership-level.* PRS is not subject to section 163(j) by reason of section 163(j)(3). As a result, none of PRS's business interest expense is subject to the section 163(j) limitation.

(iii) *Partner-level allocations.* Because PRS's business interest expense is not subject to the section 163(j) limitation, such business interest expense is not subject to the section 163(j) limitation at the level of either the partnership or partner. Additionally, pursuant to § 1.163(j)–6(m)(1), each partner includes its share of non-excepted trade or business items of income, gain, loss, and deduction (including business interest expense and business interest income) of PRS when calculating its ATI. Therefore, each partner increases its ATI by $10 (each partner's share of $20 of non-excepted income less each partner's share of $10 of non-excepted loss).

(iv) *Partner-level computations.* In computing its limit under section 163(j), each partner has $10 of ATI and $10 of business interest expense. Each partner's section 163(j) limit is $3 ($10 × 30 percent). Thus, each partner has $3 of deductible business interest expense. Each partner has $7 of business interest expense not allowed as a deduction that is treated as business interest expense paid or accrued by the partner in Year 2.

(14) *Example 14*—(i) *Facts.* The facts are the same as in *Example 5* in paragraph (o)(5)(i) of this section, except in Year 2 Y is not subject to section 163(j) under section 163(j)(3).

(ii) *Partnership-level.* Same analysis as *Example 5* in paragraph (o)(5)(ii) of this section.

(iii) *Partner-level allocations.* Same analysis as *Example 5* in paragraph (o)(5)(iii) of this section.

(iv) *Partner-level computations.* For X, same analysis as *Example 5* in paragraph (o)(5)(iv) of this section. Y is not subject to section 163(j) under section 163(j)(3). Thus, all $42 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from Year 1, plus $2 excess business interest expense treated as paid or accrued in Year 2) is not subject to limitation under § 1.163(j)–2(d). At the end of Year 2, Y has $3 of excess business interest expense from PRS ($5 from Year 1, less $2 treated as paid or accrued in Year 2).

(15) *Example 15*—(i) *Facts.* The facts are the same as in *Example 5* in paragraph (o)(5)(i) of this section, except in Year 2 PRS and Y become not subject to section 163(j) by reason of section 163(j)(3).

(ii) *Partnership-level.* In Year 2, PRS is not subject to section 163(j) by reason of section 163(j)(3). As a result, none of PRS's $40 of business interest expense is subject to the section 163(j) limitation at the level of either the partnership or partner.

(iii) *Partner-level allocations.* Because PRS is not subject to section 163(j) by reason of section 163(j)(3), PRS's $40 of business interest expense does not retain its character as business interest expense for purposes of section 163(j).

As a result, such business interest expense is not subject to the section 163(j) limitation at the level of either the partnership or partner. Additionally, pursuant to § 1.163(j)–6(m)(1), each partner includes its share of non-excepted trade or business items of income, gain, loss, and deduction (including business interest expense and business interest income) of PRS when calculating its ATI. As a result, X and Y each increase their ATI by $35.60. Further, because PRS is not subject to section 163(j) by reason of section 163(j)(3), the excess business interest expense from Year 1 is treated as paid or accrued by the partners pursuant to § 1.163(j)–6(m)(3). As a result, X and Y each treat their $5 of excess business interest expense from Year 1 as paid or accrued in Year 2, and increase their business interest expense by $5.

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $135.60 of ATI ($100 from its sole proprietorship, plus $35.60 ATI from PRS) and $25 of business interest expense ($20 from its sole proprietorship, plus $5 of excess business interest expense treated as paid or accrued in Year 2). X's section 163(j) limit is $40.68 ($135.60 × 30 percent). Thus, $25 of X's business interest expense is deductible business interest expense. Y is not subject to section 163(j) under section 163(j)(3). As a result, Y's business interest expense is not subject to the section 163(j) limitation. Thus, all $45 of Y's business interest expense ($20 from its sole proprietorship, plus $20 disallowed from year 1, plus $5 of excess business interest expense treated as paid or accrued in Year 2) is not subject to the section 163(j) limitation.

(16) *Example 16*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (o)(1)(i) of this section, except that PRS's only trade or business is a real property trade or business for which PRS does not make the election provided for in section 163(j)(7)(B). In Year 2, when PRS's only trade or business is still its real property trade or business, PRS makes the election provided for in section 163(j)(7)(B). Further, in Year 2, PRS has $100 of income and $40 of business interest expense. PRS allocates its items of income, gain, deduction, and loss equally between X and Y. X has $100 of ATI and $20 of business interest expense from its sole proprietorship. Y has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *Partnership-level.* In Year 2, PRS is not subject to section 163(j) because its only trade or business is an excepted trade or business. As a result, none of PRS's $40 of business interest expense is subject to the section 163(j) limitation at the level of either the partnership or partner.

(iii) *Partner-level allocations.* Because PRS is not subject to section 163(j), PRS's $40 of business interest expense does not retain its character as business interest expense for purposes of section 163(j). As a result, such business interest expense is not subject to the section 163(j) limitation at the partners' level. Pursuant to § 1.163(j)–6(m)(1), the partners do not include their respective $50 shares of income from PRS when calculating their own ATI because such $50 is excepted trade or business income.

(iv) *Partner-level computations.* X, in computing its limit under section 163(j), has $100 of ATI ($100 from its sole proprietorship) and $20 of business interest expense ($20 from its sole proprietorship). X's section 163(j) limit is $30 ($100 × 30 percent). Thus, $20 of X's business interest expense is deductible business interest expense. At the end of Year 2, X has $5 of excess business interest expense from PRS ($5 from Year 1). Y, in computing its limit under section 163(j), has $0 of ATI and $40 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from Year 1). Y's section 163(j) limit is $0. Thus, Y's $40 of business interest expense not allowed as a deduction is treated as business interest expense paid or accrued by Y in Year 3. At the end of Year 2, Y has $5 of excess business interest expense from PRS ($5 from Year 1).

(17) *Example 17: Facts.* A (an individual) and B (a corporation) own all of the interests in partnership PRS. At the beginning of Year 1, A and B each have $100 section 704(b) capital account and $100 of basis in PRS. In Year 1, PRS has $100 of ATI, $10 of investment interest income, $20 of business interest income (BII), $60 of business interest expense (BIE), and $10 of floor plan financing interest expense. PRS's ATI consists of $100 of gross income and $0 of gross deductions. PRS allocates its items comprising ATI $100 to A and $0 to B. PRS allocates its business interest income $10 to A and $10 to B. PRS allocates its business interest expense $30 to A and $30 to B. PRS allocates all $10 of its investment interest income and all $10 of its floor plan financing interest expense to B. A has ATI from a sole proprietorship, unrelated to PRS, in the amount of $300.

(i) First, PRS determines its limitation pursuant to § 1.163(j)–2. PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $50 (($100 × 30 percent) + $20). Thus, PRS has $0 of excess business interest income (EBII), $0 of excess taxable income, $50 of deductible business interest expense, and $10 of excess business interest expense. PRS takes its $10 of floor plan financing into account in determining its nonseparately stated taxable income or loss.

(ii) Second, PRS determines each partner's allocable share of section 163(j) items used in its own section 163(j) calculation. B's $10 of investment interest income is not included in B's allocable business interest income amount because the $10 of investment interest income was not taken into account in PRS's section 163(j) calculation. B's $10 of floor plan financing interest expense is not included in B's allocable business interest expense. The $300 of ATI from A's sole proprietorship is not included in A's allocable ATI amount because the $300 was not taken into account in PRS's section 163(j) calculation.

TABLE 1 TO PARAGRAPH (o)(17)(ii)

	A	B	Total
Allocable ATI	$100	$0	$100
Allocable BII	10	10	20
Allocable BIE	30	30	60

(iii) Third, PRS compares each partner's allocable business interest income to such partner's allocable business interest expense. Because each partner's allocable business interest expense exceeds its allocable business interest income by $20 ($30 − $10), each partner has an allocable business interest income deficit of $20. Thus, the total allocable business interest income deficit is $40 ($20 + $20). No partner has allocable business interest income excess because no partner has allocable business interest income in excess of its allocable business interest expense. Thus, the total allocable business interest income excess is $0.

TABLE 2 TO PARAGRAPH (o)(17)(iii)

	A	B	Total
Allocable BII	$10	$10	N/A
Allocable BIE	30	30	N/A
If allocable BII exceeds allocable BIE, then such amount = Allocable BII excess	0	0	$0
If allocable BIE exceeds allocable BII, then such amount = Allocable BII deficit	20	20	40

(iv) Fourth, PRS determines each partner's final allocable business interest income excess. Because no partner had any allocable business interest income excess, each partner has final allocable business interest income excess of $0.

(v) Fifth, PRS determines each partner's remaining business interest expense. PRS determines A's remaining business interest expense by reducing, but not below $0, A's allocable business interest income deficit ($20) by the product of the total allocable business interest income excess ($0) and the ratio of A's allocable business interest income deficit to the total business interest income deficit ($20/$40). Therefore, A's allocable business interest income deficit of $20 is reduced by $0 ($0 × 50 percent). As a result, A's remaining business interest expense is $20. PRS determines B's remaining business interest expense by reducing, but not below $0, B's allocable business interest income deficit ($20) by the product of the total allocable business interest income excess ($0) and the ratio of B's allocable business interest income deficit to the total business interest income deficit ($20/$40). Therefore, B's allocable business interest income deficit of $20 is reduced by $0 ($0 × 50 percent). As a result, B's remaining business interest expense is $20.

TABLE 3 TO PARAGRAPH (o)(17)(v)

	A	B	Total
Allocable BII deficit	$20	$20	$40
Less: (Total allocable BII excess) × (Allocable BII deficit/Total allocable BII deficit)	0	0	N/A
= Remaining BIE	20	20	40

(vi) Sixth, PRS determines each partner's final allocable ATI. Any partner with a negative allocable ATI, or an allocable ATI of $0, has a positive allocable ATI of $0. Therefore, B has a positive allocable ATI of $0. Because A's allocable ATI is comprised of $100 of income and gain and $0 of deduction and loss, A has positive allocable ATI of $100. Thus, the total positive allocable ATI is $100 ($100 + $0). PRS determines A's final allocable ATI by reducing, but not below $0, A's positive allocable ATI ($100) by the product of total negative allocable ATI ($0) and the ratio of A's positive allocable ATI to the total positive allocable ATI ($100/$100). Therefore, A's positive allocable ATI is reduced by $0 ($0 × 100 percent). As a result, A's final allocable ATI is $100. Because B has a positive allocable ATI of $0, B's final allocable ATI is $0.

TABLE 4 TO PARAGRAPH (o)(17)(vi)

	A	B	Total
Allocable ATI	$100	$0	$100
If deduction and loss items comprising allocable ATI exceed income and gain items comprising allocable ATI, then such excess amount = Negative allocable ATI	0	0	0
If income and gain items comprising allocable ATI equal or exceed deduction and loss items comprising allocable ATI, then such amount = Positive allocable ATI	100	0	100

TABLE 5 TO PARAGRAPH (o)(17)(vi)

	A	B	Total
Positive allocable ATI	$100	$0	$100
Less: (Total negative allocable ATI) × (Positive allocable ATI/Total positive allocable ATI)	0	0	N/A
= Final allocable ATI	100	0	100

(vii) Seventh, PRS compares each partner's ATI capacity (ATIC) amount to such partner's remaining business interest expense. A's ATIC amount is $30 ($100 × 30 percent) and B's ATIC amount is $0 ($0 × 30 percent). Because A's ATIC amount exceeds its remaining business interest expense by $10 ($30 − $20), A has an ATIC excess of $10. B does not have any ATIC excess. Thus, the total ATIC excess is $10 ($10 + $0). A does not have any ATIC deficit. Because B's remaining business interest expense exceeds its ATIC amount by $20 ($20 − $0), B has an ATIC deficit of $20. Thus, the total ATIC deficit is $20 ($0 + $20).

TABLE 6 TO PARAGRAPH (o)(17)(vii)

	A	B	Total
ATIC (Final allocable ATI × 30 percent)	$30	$0	N/A
Remaining BIE	20	20	N/A
If ATIC exceeds remaining BIE, then such excess = ATIC excess	10	0	$10
If remaining BIE exceeds ATIC, then such excess = ATIC deficit	0	20	20

(viii)(A) Eighth, PRS must perform the calculations and make the necessary adjustments described under paragraph (f)(2)(viii) of this section if, and only if, PRS has—

(*1*) An excess business interest expense greater than $0 under paragraph (f)(2)(i) of this section;

(*2*) A total negative allocable ATI greater than $0 under paragraph (f)(2)(vi) of this section; and

(*3*) A total ATIC excess amount greater than $0 under paragraph (f)(2)(vii) of this section.

(B) Because PRS does not meet all three requirements in paragraph (o)(17)(viii)(A) of this section, PRS does not perform the calculations or adjustments described in paragraph (f)(2)(viii) of this section. In sum, the correct amounts to be used in paragraphs (o)(17)(ix) and (x) of this section are as follows.

TABLE 7 TO PARAGRAPH (o)(17)(viii)(B)

	A	B	Total
ATIC excess	$10	$0	$10
ATIC deficit	0	20	20

(ix) Ninth, PRS determines each partner's final ATIC excess amount. Because A has an ATIC excess, PRS must determine A's final ATIC excess amount. A's final ATIC excess amount is A's ATIC excess ($10), reduced, but not below $0, by the product of the total ATIC deficit ($20) and the ratio of A's ATIC excess to the total ATIC excess ($10/$10). Therefore, A has $0 of final ATIC excess ($10 − ($20 × 100 percent)).

TABLE 8 TO PARAGRAPH (o)(17)(ix)

	A	B	Total
ATIC excess	$10	$0	N/A
Less: (Total ATIC deficit) × (ATIC excess/Total ATIC excess)	20	0	N/A
= Final ATIC excess	0	0	$0

(x) Tenth, PRS determines each partner's final ATIC deficit amount. Because B has an ATIC deficit, PRS must determine B's final ATIC deficit amount. B's final ATIC deficit amount is B's ATIC deficit ($20), reduced, but not below $0, by the product of the total ATIC excess ($10) and the ratio of B's ATIC deficit to the total ATIC deficit ($20/$20). Therefore, B has $10 of final ATIC deficit ($20 − ($10 × 100 percent)).

TABLE 9 TO PARAGRAPH (o)(17)(x)

	A	B	Total
ATIC deficit	$0	$20	N/A
Less: (Total ATIC excess) × (ATIC deficit/Total ATIC deficit)	0	10	N/A
= Final ATIC deficit	0	10	$10

(xi) Eleventh, PRS allocates deductible business interest expense and section 163(j) excess items to the partners. Pursuant to paragraph (f)(2)(i) of this section, PRS has $10 of excess business interest expense. PRS allocates the excess business interest expense dollar for dollar to the partners with final ATIC deficits amounts. Thus, PRS allocates all $10 of its excess business interest expense to B. A partner's allocable business interest expense is deductible business interest expense to the extent it exceeds such partner's share of excess business interest expense. Therefore, A has deductible business interest expense of $30 ($30 − $0) and B has deductible business interest expense of $20 ($30 − $10). As a result of its allocations from PRS, A increases its section 704(b) capital account and basis in PRS by $80 to $180. As a result of its allocations from PRS, B decreases its capital account and basis in PRS by $20 to $80.

TABLE 10 TO PARAGRAPH (o)(17)(xi)

	A	B	Total
Deductible BIE	$30	$20	$50

TABLE 10 TO PARAGRAPH (o)(17)(xi)—Continued

	A	B	Total
EBIE allocated	0	10	10
ETI allocated	0	0	0
EBII allocated	0	0	0

(18) *Example 18: Facts.* A, B, and C own all of the interests in partnership PRS. In Year 1, PRS has $150 of ATI, $10 of business interest income, and $40 of business interest expense. PRS's ATI consists of $200 of gross income and $50 of gross deductions. PRS allocates its items comprising ATI ($50) to A, $200 to B, and $0 to C. PRS allocates its business interest income $0 to A, $0 to B, and $10 to C. PRS allocates its business interest expense $30 to A, $10 to B, and $0 to C.

(i) First, PRS determines its limitation pursuant to § 1.163(j)–2. PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $55 (($150 × 30 percent) + $10). Thus, PRS has $0 of excess business interest income, $50 of excess taxable income, $40 of deductible business interest expense, and $0 of excess business interest expense.

(ii) Second, PRS determines each partner's allocable share of section 163(j) items used in its own section 163(j) calculation.

TABLE 11 TO PARAGRAPH (o)(18)(ii)

	A	B	C	Total
Allocable ATI	($50)	$200	$0	$150
Allocable BII	0	0	10	10
Allocable BIE	30	10	0	40

(iii) Third, PRS compares each partner's allocable business interest income to such partner's allocable business interest expense. Because A's allocable business interest expense exceeds its allocable business interest income by $30 ($30 − $0), A has an allocable business interest income deficit of $30. Because B's allocable business interest expense exceeds its allocable business interest income by $10 ($10 − $0), B has an allocable business interest income deficit of $10. C does not have any allocable business interest income deficit. Thus, the total allocable business interest income deficit is $40 ($30 + $10 + $0). A and B do not have any allocable business interest income excess. Because C's allocable business interest income exceeds its allocable business interest expense by $10 ($10 − $0), C has an allocable business interest income excess of $10. Thus, the total allocable business interest income excess is $10 ($0 + $0 + $10).

TABLE 12 TO PARAGRAPH (o)(18)(iii)

	A	B	C	Total
Allocable BII	$0	$0	$10	N/A
Allocable BIE	30	10	0	N/A
If allocable BII exceeds allocable BIE, then such amount = Allocable BII excess	0	0	10	$10
If allocable BIE exceeds allocable BII, then such amount = Allocable BII deficit	30	10	0	40

(iv) Fourth, PRS determines each partner's final allocable business interest income excess. Because A and B do not have any allocable business interest income excess, each partner has final allocable business interest income excess of $0. PRS determines C's final allocable business interest income excess by reducing, but not below $0, C's allocable business interest income excess ($10) by the product of the total allocable business interest income deficit ($40) and the ratio of C's allocable business interest income excess to the total allocable business interest income excess ($10/$10). Therefore, C's allocable business interest income excess of $10 is reduced by $10 ($40 × 100 percent). As a result, C's allocable business interest income excess is $0.

TABLE 13 TO PARAGRAPH (o)(18)(iv)

	A	B	C	Total
Allocable BII excess	$0	$0	$10	N/A
Less: (Total allocable BII deficit) × (Allocable BII excess/Total allocable BII excess)	0	0	40	N/A
= Final Allocable BII Excess	0	0	0	$10

(v) Fifth, PRS determines each partner's remaining business interest expense. PRS determines A's remaining business interest expense by reducing, but not below $0, A's allocable business interest income deficit ($30) by the product of the total allocable business interest income excess ($10) and the ratio of A's allocable business interest income deficit to the total business interest income deficit ($30/$40). Therefore, A's allocable business interest income deficit of $30 is reduced by $7.50 ($10 × 75 percent). As a result, A's remaining business interest expense is $22.50. PRS determines B's remaining business interest expense by reducing, but not below $0, B's allocable business interest income deficit ($10) by the product of the total allocable business interest income excess ($10) and the ratio of B's allocable business interest income deficit to the total business interest income deficit ($10/$40). Therefore, B's allocable business interest income deficit of $10 is reduced by $2.50 ($10 × 25 percent). As a result, B's remaining business interest expense is $7.50. Because C does not have any allocable business interest income deficit, C's remaining business interest expense is $0.

TABLE 14 TO PARAGRAPH (o)(18)(v)

	A	B	C	Total
Allocable BII deficit	$30	$10	$0	$40
Less: (Total allocable BII excess) × (Allocable BII deficit/Total allocable BII deficit)	7.50	2.50	0	N/A
= Remaining BIE	22.50	7.50	0	N/A

(vi) Sixth, PRS determines each partner's final allocable ATI. Because A's allocable ATI is comprised of $50 of items of deduction and loss and $0 of income and gain, A has negative allocable ATI of $50. A is the only partner with negative allocable ATI. Thus, the total negative allocable ATI amount is $50. Any partner with a negative allocable ATI, or an allocable ATI of $0, has a positive allocable ATI of $0. Therefore, A and C have a positive allocable ATI of $0. Because B's allocable ATI is comprised of $200 of items of income and gain and $0 of deduction and loss, B has positive allocable ATI of $200. Thus, the total positive allocable ATI is $200 ($0 + $200 + $0). PRS determines B's final allocable ATI by reducing, but not below $0, B's positive allocable ATI ($200) by the product of total negative allocable ATI ($50) and the ratio of B's positive allocable ATI to the total positive allocable ATI ($200/$200). Therefore, B's positive allocable ATI is reduced by $50 ($50 × 100 percent). As a result, B's final allocable ATI is $150.

TABLE 15 TO PARAGRAPH (o)(18)(vi)

	A	B	C	Total
Allocable ATI	($50)	$200	$0	$150
If deduction and loss items comprising allocable ATI exceed income and gain items comprising allocable ATI, then such excess amount = Negative allocable ATI	50	0	0	50
If income and gain items comprising allocable ATI equal or exceed deduction and loss items comprising allocable ATI, then such amount = Positive allocable ATI	0	200	0	200

TABLE 16 TO PARAGRAPH (o)(18)(vi)

	A	B	C	Total
Positive allocable ATI	$0	$200	$0	$200
Less: (Total negative allocable ATI) × (Positive allocable ATI/Total positive allocable ATI)	0	50	0	N/A
= Final allocable ATI	0	150	0	150

(vii) Seventh, PRS compares each partner's ATI capacity (ATIC) amount to such partner's remaining business interest expense. A's ATIC amount is $0 ($0 × 30 percent), B's ATIC amount is $45 ($150 × 30 percent), and C's ATIC amount is $0 ($0 × 30 percent). A does not have any ATIC excess. Because B's ATIC amount exceeds its remaining business interest expense by $37.50 ($45 − $7.50), B has an ATIC excess amount of $37.50. C does not have any ATIC excess. Thus, the total ATIC excess amount is $37.50 ($0 + $37.50 + $0). Because A's remaining business interest expense exceeds its ATIC amount by $22.50 ($22.50 − $0), A has an ATIC deficit of $22.50. B and C do not have any ATIC deficit. Thus, the total ATIC deficit is $22.50 ($22.50 + $0 + $0).

TABLE 17 TO PARAGRAPH (o)(18)(vii)

	A	B	C	Total
ATIC (Final allocable ATI × 30 percent)	$0	$45	$0	N/A
Remaining BIE	22.50	7.50	0	N/A
If ATIC exceeds remaining BIE, then such excess = ATIC excess	0	37.50	0	$37.50
If remaining BIE exceeds ATIC, then such excess = ATIC deficit	22.50	0	0	22.50

(viii)(A) Eighth, PRS must perform the calculations and make the necessary adjustments described under paragraph (f)(2)(viii) of this section if, and only if, PRS has—

(*1*) An excess business interest expense greater than $0 under paragraph (f)(2)(i) of this section;

(*2*) A total negative allocable ATI greater than $0 under paragraph (f)(2)(vi) of this section; and

(*3*) A total ATIC excess amount greater than $0 under paragraph (f)(2)(vii) of this section.

(B) Because PRS does not meet all three requirements in paragraph (o)(18)(viii)(A) of this section, PRS does not perform the calculations or adjustments described in paragraph (f)(2)(viii) of this section. In sum, the correct amounts to be used in paragraphs (o)(18)(ix) and (x) of this section are as follows.

TABLE 18 TO PARAGRAPH (o)(18)(viii)(B)

	A	B	C	Total
ATIC excess	$0	$37.50	$0	$37.50
ATIC deficit	22.50	0	0	22.50

(ix) Ninth, PRS determines each partner's final ATIC excess amount. Because B has ATIC excess, PRS must determine B's final ATIC excess amount. B's final ATIC excess amount is B's ATIC excess ($37.50), reduced, but not below $0, by the product of the total ATIC deficit ($22.50) and the ratio of B's ATIC excess to the total ATIC excess ($37.50/$37.50). Therefore, B has $15 of final ATIC excess ($37.50 − ($22.50 × 100 percent)).

TABLE 19 TO PARAGRAPH (o)(18)(ix)

	A	B	C	Total
ATIC excess	$0	$37.50	$0	N/A
Less: (Total ATIC deficit) × (ATIC excess/Total ATIC excess)	0	22.50	0	N/A
= Final ATIC excess	0	15	0	$15

(x) Tenth, PRS determines each partner's final ATIC deficit amount. Because A has an ATIC deficit, PRS must determine A's final ATIC deficit amount. A's final ATIC deficit amount is A's ATIC deficit ($22.50), reduced, but not below $0, by the product of the total ATIC excess ($37.50) and the ratio of A's ATIC deficit to the total ATIC deficit ($22.50/$22.50). Therefore, A has $0 of final ATIC deficit ($22.50 − ($37.50 × 100 percent)).

TABLE 20 TO PARAGRAPH (o)(18)(x)

	A	B	C	Total
ATIC deficit	$22.50	$0	$0	N/A
Less: (Total ATIC excess) × (ATIC deficit/Total ATIC deficit)	37.50	0	0	N/A
= Final ATIC deficit	0	0	0	0

(xi) Eleventh, PRS allocates deductible business interest expense and section 163(j) excess items to the partners. Pursuant to paragraph (f)(2)(i) of this section, PRS has $50 of excess taxable income and $40 of deductible business interest expense. After grossing up each partner's final ATIC excess amounts by ten-thirds, excess taxable income is allocated dollar for dollar to partners with final ATIC excess amounts. Thus, PRS allocates its excess taxable income $50 to B. A partner's allocable business interest expense is deductible business interest expense to the extent it exceeds such partner's share of excess business interest expense. Therefore, A has deductible business interest expense of $30 ($30 − $0), B has deductible business interest expense of $10 ($10 − $0), and C has deductible business interest expense of $0 ($0 − $0).

TABLE 21 TO PARAGRAPH (o)(18)(xi)

	A	B	C	Total
Deductible BIE	$30	$10	$0	$40
EBIE allocated	0	0	0	0
ETI allocated	0	50	0	50
EBII allocated	0	0	0	0

(19) *Example 19: Facts.* A, B, and C own all of the interests in partnership PRS. In Year 1, PRS has $100 of ATI, $0 of business interest income, and $50 of business interest expense. PRS's ATI consists of $200 of gross income and $100 of gross deductions. PRS allocates its items comprising ATI $100 to A, $100 to B, and ($100) to C. PRS allocates its business interest expense $0 to A, $25 to B, and $25 to C.

(i) First, PRS determines its limitation pursuant to § 1.163(j)–2. PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $30 ($100 × 30 percent). Thus, PRS has $30 of deductible business interest expense and $20 of excess business interest expense.

(ii) Second, PRS determines each partner's allocable share of section 163(j) items used in its own section 163(j) calculation.

TABLE 22 TO PARAGRAPH (o)(19)(ii)

	A	B	C	Total
Allocable ATI	$100	$100	($100)	$100
Allocable BII	0	0	0	0
Allocable BIE	0	25	25	50

(iii) Third, PRS compares each partner's allocable business interest income to such partner's allocable business interest expense. No partner has allocable business interest income. Consequently, each partner's allocable business interest income deficit is equal to such partner's allocable business interest expense. Thus, A's allocable business interest income deficit is $0, B's allocable business interest income deficit is $25, and C's allocable business interest income deficit is $25. The total allocable business interest income deficit is $50 ($0 + $25 + $25). No partner has allocable business interest income excess because no partner has allocable business interest income in excess of its allocable business interest expense. Thus, the total allocable business interest income excess is $0.

TABLE 23 TO PARAGRAPH (o)(19)(iii)

	A	B	C	Total
Allocable BII	$0	$0	$0	N/A
Allocable BIE	0	25	25	N/A
If allocable BII exceeds allocable BIE, then such amount = Allocable BII excess	0	0	0	$0
If allocable BIE exceeds allocable BII, then such amount = Allocable BII deficit	0	25	25	50

(iv) Fourth, PRS determines each partner's final allocable business interest income excess. Because no partner had any allocable business interest income excess, each partner has final allocable business interest income excess of $0.

(v) Fifth, PRS determines each partner's remaining business interest expense. Because no partner has any allocable business interest income excess, each partner's remaining business interest expense equals its allocable business interest income deficit. Thus, A's remaining business interest expense is $0, B's remaining business interest expense is $25, and C's remaining business interest expense is $25.

TABLE 24 TO PARAGRAPH (o)(19)(v)

	A	B	C	Total
Allocable BII deficit	$0	$25	$25	$50
Less: (Total allocable BII excess) × (Allocable BII deficit/Total allocable BII deficit)	0	0	0	N/A
= Remaining BIE	0	25	25	N/A

(vi) Sixth, PRS determines each partner's final allocable ATI. Because C's allocable ATI is comprised of $100 of items of deduction and loss and $0 of income and gain, C has negative allocable ATI of $100. C is the only partner with negative allocable ATI. Thus, the total negative allocable ATI amount is $100. Any partner with a negative allocable ATI, or an allocable ATI of $0, has a positive allocable ATI of $0. Therefore, C has a positive allocable ATI of $0. Because A's allocable ATI is comprised of $100 of items of income and gain and $0 of deduction and loss, A has positive allocable ATI of $100. Because B's allocable ATI is comprised of $100 of items of income and gain and $0 of deduction and loss, B has positive allocable ATI of $100. Thus, the total positive allocable ATI is $200 ($100 + $100 + $0). PRS determines A's final allocable ATI by reducing, but not below $0, A's positive allocable ATI ($100) by the product of total negative allocable ATI ($100) and the ratio of A's positive allocable ATI to the total positive allocable ATI ($100/$200). Therefore, A's positive allocable ATI is reduced by $50 ($100 × 50 percent). As a result, A's final allocable ATI is $50. PRS determines B's final allocable ATI by reducing, but not below $0, B's positive allocable ATI ($100) by the product of total negative allocable ATI ($100) and the ratio of B's positive allocable ATI to the total positive allocable ATI ($100/$200). Therefore, B's positive allocable ATI is reduced by $50 ($100 × 50 percent). As a result, B's final allocable ATI is $50. Because C has a positive allocable ATI of $0, C's final allocable ATI is $0.

TABLE 25 TO PARAGRAPH (o)(19)(vi)

	A	B	C	Total
Allocable ATI	$100	$100	($100)	$100
If deduction and loss items comprising allocable ATI exceed income and gain items comprising allocable ATI, then such excess amount = Negative allocable ATI	0	0	100	100
If income and gain items comprising allocable ATI equal or exceed deduction and loss items comprising allocable ATI, then such amount = Positive allocable ATI	100	100	0	200

TABLE 26 TO PARAGRAPH (o)(19)(vi)

	A	B	C	Total
Positive allocable ATI	$100	$100	$0	$200
Less: (Total negative allocable ATI) × (Positive allocable ATI/Total positive allocable ATI)	50	50	0	N/A
= Final allocable ATI	50	50	0	100

(vii) Seventh, PRS compares each partner's ATI capacity (ATIC) amount to such partner's remaining business interest expense. A's ATIC amount is $15 ($50 × 30 percent), B's ATIC amount is $15 ($50 × 30 percent), and C's ATIC amount is $0 ($0 × 30 percent). Because A's ATIC amount exceeds its remaining business interest expense by $15 ($15 − $0), A has an ATIC excess of $15. B and C do not have any ATIC excess. Thus, the total ATIC excess is $15 ($15 + $0 + $0). A does not have any ATIC deficit. Because B's remaining business interest expense exceeds its ATIC amount by $10 ($25 − $15), B has an ATIC deficit of $10. Because C's remaining business interest expense exceeds its ATIC amount by $25 ($25 − $0), C has an ATIC deficit of $25. Thus, the total ATIC deficit is $35 ($0 + $10 + $25).

TABLE 27 TO PARAGRAPH (o)(19)(vii)

	A	B	C	Total
ATIC (Final allocable ATI × 30 percent)	$15	$15	$0	N/A
Remaining BIE	0	25	25	N/A
If ATIC exceeds remaining BIE, then such excess = ATIC excess	15	0	0	$15
If remaining BIE exceeds ATIC, then such excess = ATIC deficit	0	10	25	35

(viii)(A) Eighth, PRS must perform the calculations and make the necessary adjustments described under paragraph (f)(2)(viii) of this section if, and only if, PRS has—

(*1*) An excess business interest expense greater than $0 under paragraph (f)(2)(i) of this section;

(*2*) A total negative allocable ATI greater than $0 under paragraph (f)(2)(vi) of this section; and

(*3*) A total ATIC excess greater than $0 under paragraph (f)(2)(vii) of this section. Because PRS satisfies each of these three requirements, PRS must perform the calculations and make the necessary adjustments described under paragraphs (f)(2)(viii)(B) and (C) or (D) of this section.

(B) PRS must determine each partner's priority amount and usable priority amount. Only partners with an ATIC deficit under paragraph (f)(2)(vii) of this section can have a priority amount greater than $0. Thus, only partners B and C can have a priority amount greater than $0. PRS determines a partner's priority amount as 30 percent of the amount by which such partner's allocable positive ATI exceeds its final allocable ATI. Therefore, A's priority amount is $0, B's priority amount is $15 (($100 − $50) × 30 percent), and C's priority amount is $0 (($0 − $0) × 30 percent). Thus, the total priority amount is $15 ($0 + $15 + $0). Next, PRS must determine each partner's usable priority amount. Each partner's usable priority amount is the lesser of such partner's priority amount or ATIC deficit. Thus, A has a usable priority amount of $0, B has a usable priority amount of $10, and C has a usable priority amount of $0. As a result, the total usable priority amount is $10 ($0 + $10 + $0). Because the total ATIC excess under paragraph (f)(2)(vii) of this section ($15) is greater than the total usable priority amount ($10), PRS must perform the adjustments described in paragraph (f)(2)(viii)(C) of this section.

TABLE 28 TO PARAGRAPH (o)(19)(viii)(B)

	A	B	C	Total
(Positive allocable ATI—Final allocable ATI)	$0	$50	$0	N/A
Multiplied by 30 percent	30%	30%	30%	N/A
= Priority amount	$0	$15	$0	$15

TABLE 29 TO PARAGRAPH (o)(19)(viii)(B)

	A	B	C	Total
Priority amount	$0	$15	$0	N/A
ATIC deficit	0	10	25	N/A
Lesser of priority amount or ATIC deficit = Usable priority amount	0	10	0	$10

(C) For purposes of paragraph (f)(2)(ix) of this section, each partner's final ATIC excess is $0. For purposes of paragraph (f)(2)(x) of this section, the following terms have the following meanings. Each partner's ATIC deficit is such partner's ATIC deficit as determined pursuant to paragraph (f)(2)(vii) of this section reduced by such partner's usable priority amount. Thus, A's ATIC deficit is $0 ($0 − $0), B's ATIC deficit is $0 ($10 − $10), and C's ATIC deficit is $25 ($25 − $0). The total ATIC deficit is the total ATIC deficit determined pursuant to paragraph (f)(2)(vii) ($35) reduced by the total usable priority amount ($10). Thus, the total ATIC deficit is $25 ($35 − $10). The total ATIC excess is the total ATIC excess determined pursuant to paragraph (f)(2)(vii) of this section ($15) reduced by the total usable priority amount ($10). Thus, the total ATIC excess is $5 ($15 − $5).

TABLE 30 TO PARAGRAPH (o)(19)(viii)(C)

	A	B	C	Total
ATIC deficit	$0	$10	$25	N/A
Less: Usable priority amount	0	10	0	N/A
= ATIC deficit for purposes of paragraph (f)(2)(x) of this section	0	0	25	$25

(D)(1) In light of the fact that the total ATIC excess was greater than the total usable priority amount under paragraph (f)(2)(viii)(B) of this section, paragraph (f)(2)(viii)(D) of this section does not apply.

(2) In sum, the correct amounts to be used in paragraphs (o)(19)(ix) and (x) of this section are as follows.

TABLE 31 TO PARAGRAPH (o)(19)(viii)(D)(2)

	A	B	C	Total
ATIC excess	$5	$0	$0	$5
ATIC deficit	0	0	25	25

(ix) Ninth, PRS determines each partner's final ATIC excess amount. Pursuant to paragraph (f)(2)(viii)(C) of this section, each partner's final ATIC excess amount is $0.

(x) Tenth, PRS determines each partner's final ATIC deficit amount. Because C has an ATIC deficit, PRS must determine C's final ATIC deficit amount. C's final ATIC deficit amount is C's ATIC deficit ($25), reduced, but not below $0, by the product of the total ATIC excess ($5) and the ratio of C's ATIC deficit to the total ATIC deficit ($25/$25). Therefore, C has $20 of final ATIC deficit ($25 − ($5 × 100 percent)).

TABLE 32 TO PARAGRAPH (o)(19)(x)

	A	B	C	Total
ATIC deficit	$0	$0	$25	N/A
Less: (Total ATIC excess) × (ATIC deficit/Total ATIC deficit)	0	0	5	N/A
= Final ATIC deficit	0	0	20	$20

(xi) Eleventh, PRS allocates deductible business interest expense and section 163(j) excess items to the partners. Pursuant to paragraph (f)(2)(i) of this section, PRS has $20 of excess business interest expense. PRS allocates the excess business interest expense dollar for dollar to the partners with final ATIC deficits. Thus, PRS allocates its excess business interest expense $20 to C. A partner's allocable business interest expense is deductible business interest expense to the extent it exceeds such partner's share of excess business interest expense. Therefore, A has deductible business interest expense of $0 ($0 − $0), B has deductible business interest expense of $25 ($25 − $0), and C has deductible business interest expense of $5 ($25 − $20).

TABLE 33 TO PARAGRAPH (o)(19)(xi)

	A	B	C	Total
Deductible BIE	$0	$25	$5	$30
EBIE allocated	0	0	20	20
ETI allocated	0	0	0	0

TABLE 33 TO PARAGRAPH (o)(19)(xi)—Continued

	A	B	C	Total
EBII allocated	0	0	0	0

(20) *Example 20: Facts.* A, B, C, and D own all of the interests in partnership PRS. In Year 1, PRS has $200 of ATI, $0 of business interest income, and $140 of business interest expense. PRS's ATI consists of $600 of gross income and $400 of gross deductions. PRS allocates its items comprising ATI $100 to A, $100 to B, $400 to C, and ($400) to D. PRS allocates its business interest expense $0 to A, $40 to B, $60 to C, and $40 to D.

(i) First, PRS determines its limitation pursuant to § 1.163(j)–2. PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $60 ($200 × 30 percent). Thus, PRS has $60 of deductible business interest expense and $80 of excess business interest expense.

(ii) Second, PRS determines each partner's allocable share of section 163(j) items used in its own section 163(j) calculation.

TABLE 34 TO PARAGRAPH (o)(20)(ii)

	A	B	C	D	Total
Allocable ATI	$100	$100	$400	($400)	$200
Allocable BII	0	0	0	0	0
Allocable BIE	0	40	60	40	140

(iii) Third, PRS compares each partner's allocable business interest income to such partner's allocable business interest expense. No partner has allocable business interest income. Consequently, each partner's allocable business interest income deficit is equal to such partner's allocable business interest expense. Thus, A's allocable business interest income deficit is $0, B's allocable business interest income deficit is $40, C's allocable business interest income deficit is $60, and D's allocable business interest income deficit is $40. The total allocable business interest income deficit is $140 ($0 + $40 + $60 + $40). No partner has allocable business interest income excess because no partner has allocable business interest income in excess of its allocable business interest expense. Thus, the total allocable business interest income excess is $0.

TABLE 35 TO PARAGRAPH (o)(20)(iii)

	A	B	C	D	Total
Allocable BII	$0	$0	$0	$0	N/A
Allocable BIE	0	40	60	40	N/A
If allocable BII exceeds allocable BIE, then such amount = Allocable BII excess	0	0	0	0	$0
If allocable BIE exceeds allocable BII, then such amount = Allocable BII deficit	0	40	60	40	140

(iv) Fourth, PRS determines each partner's final allocable business interest income excess. Because no partner has any allocable business interest income excess, each partner has final allocable business interest income excess of $0.

(v) Fifth, PRS determines each partner's remaining business interest expense. Because no partner has any allocable business interest income excess, each partner's remaining business interest expense equals its allocable business interest income deficit. Thus, A's remaining business interest expense is $0, B's remaining business interest expense is $40, C's remaining business interest expense is $60, and D's remaining business interest expense is $40.

TABLE 36 TO PARAGRAPH (o)(20)(v)

	A	B	C	D	Total
Allocable BII deficit	$0	$40	$60	$40	$140
Less: (Total allocable BII excess) × (Allocable BII deficit/ Total allocable BII deficit)	0	0	0	0	N/A
= Remaining BIE	0	40	60	40	N/A

(vi) Sixth, PRS determines each partner's final allocable ATI. Because D's allocable ATI is comprised of $400 of items of deduction and loss and $0 of income and gain, D has negative allocable ATI of $400. D is the only partner with negative allocable ATI. Thus, the total negative allocable ATI amount is $400. Any partner with a negative allocable ATI, or an allocable ATI of $0, has a positive allocable ATI of $0. Therefore, D has a positive allocable ATI of $0. PRS determines A's final allocable ATI by reducing, but not below $0, A's positive allocable ATI ($100) by the product of total negative allocable ATI ($400) and the ratio of A's positive allocable ATI to the total positive allocable ATI ($100/$600). Therefore, A's positive allocable ATI is reduced by $66.67 ($400 × 16.67 percent). As a result, A's final allocable ATI is $33.33. PRS determines B's final allocable ATI by reducing, but not below $0, B's positive allocable ATI ($100) by the product of total negative allocable ATI ($400) and the ratio of B's positive allocable ATI to the total positive allocable ATI ($100/$600). Therefore, B's positive allocable ATI is reduced by $66.67 ($400 × 16.67 percent). As a result, B's final allocable ATI is $33.33. PRS determines C's final allocable ATI by reducing, but not below $0, C's positive allocable ATI ($400) by the product of total negative allocable ATI ($400) and the ratio of C's positive allocable ATI to the total positive allocable ATI ($400/$600). Therefore, C's positive allocable ATI is reduced by $266.67 ($400 × 66.67 percent). As a result, C's final allocable ATI is $133.33. Because D has a positive allocable ATI of $0, D's final allocable ATI is $0.

TABLE 37 TO PARAGRAPH (o)(20)(vi)

	A	B	C	D	Total
Allocable ATI	$100	$100	$400	($400)	$200
If deduction and loss items comprising allocable ATI exceed income and gain items comprising allocable ATI, then such excess amount = Negative allocable ATI	0	0	0	400	400
If income and gain items comprising allocable ATI equal or exceed deduction and loss items comprising allocable ATI, then such amount = Positive allocable ATI	100	100	400	0	600

TABLE 38 TO PARAGRAPH (o)(20)(vi)

	A	B	C	D	Total
Positive allocable ATI	$100	$100	$400	$0	$600
Less: (Total negative allocable ATI) × (Positive allocable ATI/Total positive allocable ATI)	66.67	66.67	266.67	0	N/A
= Final allocable ATI	33.33	33.33	133.33	0	200

(vii) Seventh, PRS compares each partner's ATI capacity (ATIC) amount to such partner's remaining business interest expense. A's ATIC amount is $10 ($33.33 × 30 percent), B's ATIC amount is $10 ($33.33 × 30 percent), C's ATIC amount is $40 ($133.33 × 30 percent), and D's ATIC amount is $0 ($0 × 30 percent). Because A's ATIC amount exceeds its remaining business interest expense by $10 ($10 − $0), A has an ATIC excess of $10. B, C, and D do not have any ATIC excess. Thus, the total ATIC excess is $10 ($10 + $0 + $0 + $0). A does not have any ATIC deficit. Because B's remaining business interest expense exceeds its ATIC amount by $30 ($40 − $10), B has an ATIC deficit of $30. Because C's remaining business interest expense exceeds its ATIC amount by $20 ($60 − $40), C has an ATIC deficit of $20. Because D's remaining business interest expense exceeds its ATIC amount by $40 ($40 − $0), D has an ATIC deficit of $40. Thus, the total ATIC deficit is $90 ($0 + $30 + $20 + $40).

TABLE 39 TO PARAGRAPH (o)(20)(vii)

—	A	B	C	D	Total
ATIC (Final allocable ATI × 30 percent)	$10	$10	$40	$0	N/A
Remaining BIE	0	40	60	40	N/A
If ATIC exceeds remaining BIE, then such excess = ATIC excess	10	0	0	0	$10
If remaining BIE exceeds ATIC, then such excess = ATIC deficit	0	30	20	40	90

(viii)(A) Eighth, PRS must perform the calculations and make the necessary adjustments described under paragraph (f)(2)(viii) of this section if, and only if, PRS has (1) an excess business interest expense greater than $0 under paragraph (f)(2)(i) of this section, (2) a total negative allocable ATI greater than $0 under paragraph (f)(2)(vi) of this section, and (3) a total ATIC excess amount greater than $0 under paragraph (f)(2)(vii) of this section. Because PRS satisfies each of these three requirements, PRS must perform the calculations and make the necessary adjustments described under paragraphs (f)(2)(viii)(B) and (C) or paragraph (f)(2)(viii)(D) of this section.

(B) PRS must determine each partner's priority amount and usable priority amount. Only partners with an ATIC deficit under paragraph (f)(2)(vii) of this section can have a priority amount greater than $0. Thus, only partners B, C, and D can have a priority amount greater than $0. PRS determines a partner's priority amount as 30 percent of the amount by which such partner's allocable positive ATI exceeds its final allocable ATI. Therefore, B's priority amount is $20 (($100 − $33.33) × 30 percent), C's priority amount is $80 (($400 − $133.33) × 30 percent), and D's priority amount is $0 (($0 − $0) × 30 percent). Thus, the total priority amount is $100 ($0 + $20 + $80 + $0). Next, PRS must determine each partner's usable priority amount. Each partner's usable priority amount is the lesser of such partner's priority amount or ATIC deficit. Thus, A has a usable priority amount of $0, B has a usable priority amount of $20, C has a usable priority amount of $20, and D has a usable priority amount of $0. As a result, the total usable priority amount is $40 ($0 + $20 + $20 + $0). Because the total usable priority amount ($40) is greater than the total ATIC excess under paragraph (f)(2)(vii) of this section ($10), PRS must perform the adjustments described in paragraph (f)(2)(viii)(D) of this section.

TABLE 40 TO PARAGRAPH (o)(20)(viii)(B)

	A	B	C	D	Total
(Positive allocable ATI—Final allocable ATI)	$0	$66.67	$266.67	$0	N/A
Multiplied by 30 percent	30%	30%	30%	30%	N/A
= Priority amount	0	20	80	0	$100

TABLE 41 TO PARAGRAPH (o)(20)(viii)(B)

	A	B	C	D	Total
Priority amount	$0	$20	$80	$0	N/A
ATIC deficit	0	30	20	40	N/A
Lesser of priority amount or ATIC deficit = Usable priority amount	0	20	20	0	$40

(C) In light of the fact that the total usable priority amount is greater than the total ATIC excess under paragraph (f)(2)(viii)(B) of this section, paragraph (f)(2)(viii)(C) of this section does not apply.

(D)(*1*) Because B and C are the only partners with priority amounts greater than $0, B and C are priority partners, while A and D are non-priority partners. For purposes of paragraph (f)(2)(ix) of this section, each partner's final ATIC excess amount is $0. For purposes of paragraph (f)(2)(x) of this section, each non-priority partner's final ATIC deficit amount is such partner's ATIC deficit determined pursuant to paragraph (f)(2)(vii) of this section. Therefore, A has a final ATIC deficit of $0 and D has a final ATIC deficit of $40. Additionally, for purposes of paragraph (f)(2)(x) of this section, PRS must determine each priority partner's step eight excess share. A priority partner's step eight excess share is the product of the total ATIC excess and the ratio of the partner's priority amount to the total priority amount. Thus, B's step eight excess share is $2 ($10 × ($20/$100)) and C's step eight excess share is $8 ($10 × ($80/$100)). To the extent a priority partner's step eight excess share exceeds its ATIC deficit, the excess will be the partner's ATIC excess for purposes of paragraph (f)(2)(x) of this section. Thus, B and C each have an ATIC excess of $0, resulting in a total ATIC excess is $0. To the extent a priority partner's ATIC deficit exceeds its step eight excess share, the excess will be the partner's ATIC deficit for purposes of paragraph (f)(2)(x) of this section. Because B's ATIC deficit ($30) exceeds its step eight excess share ($2), B's ATIC deficit for purposes of paragraph (f)(2)(x) of this section is $28 ($30 − $2). Because C's ATIC deficit ($20) exceeds its step eight excess share ($8), C's ATIC deficit for purposes of paragraph (f)(2)(x) of this section is $12 ($20 − $8). Thus, the total ATIC deficit is $40 ($28 + $12).

TABLE 42 TO PARAGRAPH (o)(20)(viii)(D)(*1*)

	A	B	C	D	Total
Non-priority partners ATIC deficit in paragraph (f)(2)(vii) = Final ATIC deficit for purposes of paragraph (f)(2)(x) of this section	$0	N/A	N/A	$40	N/A

TABLE 43 TO PARAGRAPH (o)(20)(viii)(D)(*1*)

	A	B	C	D	Total
Priority partners step eight excess share = (Total ATIC excess) × (Priority/Total priority)	N/A	$2	$8	N/A	N/A
ATIC deficit	N/A	30	20	N/A	N/A
If step eight excess share exceeds ATIC deficit, then such excess = ATIC excess for purposes of paragraph (f)(2)(x) of this section	N/A	0	0	N/A	0
If ATIC deficit exceeds step eight excess share, then such excess = ATIC deficit for purposes of paragraph (f)(2)(x) of this section	N/A	28	12	N/A	40

(*2*) In sum, the correct amounts to be used in paragraphs (o)(20)(ix) and (x) of this section are as follows.

TABLE 44 TO PARAGRAPH (o)(20)(viii)(D)(2)

	A	B	C	D	Total
ATIC excess	$0	$0	$0	$0	$0
ATIC deficit	0	28	12	0	40
Non-priority partner final ATIC deficit	0	0	0	0	N/A

(ix) Ninth, PRS determines each partner's final ATIC excess amount. Pursuant to paragraph (f)(2)(viii)(D) of this section, each priority and non-priority partner's final ATIC excess amount is $0.

(x) Tenth, PRS determines each partner's final ATIC deficit amount. Because B has an ATIC deficit, PRS must determine B's final ATIC deficit amount. B's final ATIC deficit amount is B's ATIC deficit ($28), reduced, but not below $0, by the product of the total ATIC excess ($0) and the ratio of B's ATIC deficit to the total ATIC deficit ($28/$40). Therefore, B has $28 of final ATIC deficit ($28 − ($0 × 70 percent)). Because C has an ATIC deficit, PRS must determine C's final ATIC deficit amount. C's final ATIC deficit amount is C's ATIC deficit ($12), reduced, but not below $0, by the product of the total ATIC excess ($0) and the ratio of C's ATIC deficit to the total ATIC deficit ($12/$40). Therefore, C has $12 of final ATIC deficit ($12 − ($0 × 30 percent)). Pursuant to paragraph (f)(2)(viii)(D) of this section, D's final ATIC deficit amount is $40.

TABLE 45 TO PARAGRAPH (o)(20)(x)

	A	B	C	D	Total
ATIC deficit	N/A	$28	$12	N/A	N/A
Less: (Total ATIC excess) × (ATIC deficit/Total ATIC deficit)	N/A	0	0	N/A	N/A
= Final ATIC deficit	$0	28	12	$40	$80

(xi) Eleventh, PRS allocates deductible business interest expense and section 163(j) excess items to the partners. Pursuant to paragraph (f)(2)(i) of this section, PRS has $80 of excess business interest expense. PRS allocates the excess business interest expense dollar for dollar to the partners with final ATIC deficits. Thus, PRS allocates its excess business interest expense $28 to B, $12 to C, and $40 to D. A partner's allocable business interest expense is deductible business interest expense to the extent it exceeds such partner's share of excess business interest expense. Therefore, A has deductible business interest expense of $0 ($0 − $0), B has deductible business interest expense of $12 ($40 − $28), C has deductible business interest expense of $48 ($60 − $12), and D has deductible business interest expense of $0 ($40 − $40).

TABLE 46 TO PARAGRAPH (o)(20)(xi)

	A	B	C	D	Total
Deductible BIE	$0	$12	$48	$0	$60
EBIE allocated	0	28	12	40	80
ETI allocated	0	0	0	0	0
EBII allocated	0	0	0	0	0

(21) *Example 21: Facts.* A, B, C, and D own all of the interests in partnership PRS. In Year 1, PRS has $200 of ATI, $0 of business interest income, and $150 of business interest expense. PRS's ATI consists of $500 of gross income and $300 of gross deductions. PRS allocates its items comprising ATI $50 to A, $50 to B, $400 to C, and ($300) to D. PRS allocates its business interest expense $0 to A, $50 to B, $50 to C, and $50 to D.

(i) First, PRS determines its limitation pursuant to § 1.163(j)–2. PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $60 ($200 × 30 percent). Thus, PRS has $60 of deductible business interest expense, and $90 of excess business interest expense.

(ii) Second, PRS determines each partner's allocable share of section 163(j) items used in its own section 163(j) calculation.

TABLE 47 TO PARAGRAPH (o)(21)(ii)

	A	B	C	D	Total
Allocable ATI	$50	$50	$400	($300)	$200
Allocable BII	0	0	0	0	0
Allocable BIE	0	50	50	50	150

(iii) Third, PRS compares each partner's allocable business interest income to such partner's allocable business interest expense. No partner has allocable business interest income. Consequently, each partner's allocable business interest income deficit is equal to such partner's allocable business interest expense. Thus, A's allocable business interest income deficit is $0, B's allocable business interest income deficit is $50, C's allocable business interest income deficit is $50, and D's allocable business interest income deficit is $50. The total allocable business interest income deficit is $150 ($0 + $50 + $50 + $50). No partner has allocable business interest income excess because no partner has allocable business interest income in excess of its allocable business interest expense. Thus, the total allocable business interest income excess is $0.

TABLE 48 TO PARAGRAPH (o)(21)(iii)

	A	B	C	D	Total
Allocable BII	$0	$0	$0	$0	N/A
Allocable BIE	0	50	50	50	N/A
If allocable BII exceeds allocable BIE, then such amount = Allocable BII excess	0	0	0	0	0
If allocable BIE exceeds allocable BII, then such amount = Allocable BII deficit	0	50	50	50	150

(iv) Fourth, PRS determines each partner's final allocable business interest income excess. Because no partner has any allocable business interest income excess, each partner has final allocable business interest income excess of $0.

(v) Fifth, PRS determines each partner's remaining business interest expense. Because no partner has any allocable business interest income excess, each partner's remaining business interest expense equals its allocable business interest income deficit. Thus, A's remaining business interest expense is $0, B's remaining business interest expense is $50, C's remaining business interest expense is $50, and D's remaining business interest expense is $50.

TABLE 49 TO PARAGRAPH (o)(21)(v)

	A	B	C	D	Total
Allocable BII deficit	$0	$50	$50	$50	$150
Less: (Total allocable BII excess) × (Allocable BII deficit/ Total allocable BII deficit)	0	0	0	0	N/A
= Remaining BIE	0	50	50	50	N/A

(vi) Sixth, PRS determines each partner's final allocable ATI. Because D's allocable ATI is comprised of $300 of items of deduction and loss and $0 of income and gain, D has negative allocable ATI of $300. D is the only partner with negative allocable ATI. Thus, the total negative allocable ATI amount is $300. Any partner with a negative allocable ATI, or an allocable ATI of $0, has a positive allocable ATI of $0. Therefore, D has a positive allocable ATI of $0. PRS determines A's final allocable ATI by reducing, but not below $0, A's positive allocable ATI ($50) by the product of total negative allocable ATI ($300) and the ratio of A's positive allocable ATI to the total positive allocable ATI ($50/$500). Therefore, A's positive allocable ATI is reduced by $30 ($300 × 10 percent). As a result, A's final allocable ATI is $20. PRS determines B's final allocable ATI by reducing, but not below $0, B's positive allocable ATI ($50) by the product of total negative allocable ATI ($300) and the ratio of B's positive allocable ATI to the total positive allocable ATI ($50/$500). Therefore, B's positive allocable ATI is reduced by $30 ($300 × 10 percent). As a result, B's final allocable ATI is $20. PRS determines C's final allocable ATI by reducing, but not below $0, C's positive allocable ATI ($400) by the product of total negative allocable ATI ($300) and the ratio of C's positive allocable ATI to the total positive allocable ATI ($400/$500). Therefore, C's positive allocable ATI is reduced by $240 ($300 × 80 percent). As a result, C's final allocable ATI is $160. Because D has a positive allocable ATI of $0, D's final allocable ATI is $0.

TABLE 50 TO PARAGRAPH (o)(21)(vi)

	A	B	C	D	Total
Allocable ATI	$50	$50	$400	($300)	$200
If deduction and loss items comprising allocable ATI exceed income and gain items comprising allocable ATI, then such excess amount = Negative allocable ATI	0	0	0	300	300
If income and gain items comprising allocable ATI equal or exceed deduction and loss items comprising allocable ATI, then such amount = Positive allocable ATI	50	50	400	0	500

TABLE 51 TO PARAGRAPH (o)(21)(vi)

	A	B	C	D	Total
Positive allocable ATI	$50	$50	$400	$0	$500

TABLE 51 TO PARAGRAPH (o)(21)(vi)—Continued

	A	B	C	D	Total
Less: (Total negative allocable ATI) × (Positive allocable ATI/Total positive allocable ATI)	30	30	240	0	N/A
= Final allocable ATI	20	20	160	0	200

(vii) Seventh, PRS compares each partner's ATI capacity (ATIC) amount to such partner's remaining business interest expense. A's ATIC amount is $6 ($20 × 30 percent), B's ATIC amount is $6 ($20 × 30 percent), C's ATIC amount is $48 ($160 × 30 percent), and D's ATIC amount is $0 ($0 × 30 percent). Because A's ATIC amount exceeds its remaining business interest expense by $6 ($6 − $0), A has an ATIC excess of $6. B, C, and D do not have any ATIC excess. Thus, the total ATIC excess amount is $6 ($6 + $0 + $0 + $0). A does not have any ATIC deficit. Because B's remaining business interest expense exceeds its ATIC amount by $44 ($50 − $6), B has an ATIC deficit of $44. Because C's remaining business interest expense exceeds its ATIC amount by $2 ($50 − $48), C has an ATIC deficit of $2. Because D's remaining business interest expense exceeds its ATIC amount by $50 ($50 − $0), D has an ATIC deficit of $50. Thus, the total ATIC deficit is $96 ($0 + $44 + $2 + $50).

TABLE 52 TO PARAGRAPH (o)(21)(vii)

	A	B	C	D	Total
ATIC (Final allocable ATI × 30 percent)	$6	$6	$48	$0	N/A
Remaining BIE	0	50	50	50	N/A
If ATIC exceeds remaining BIE, then such excess = ATIC excess	6	0	0	0	$6
If remaining BIE exceeds ATIC, then such excess = ATIC deficit	0	44	2	50	96

(viii)(A) Eighth, PRS must perform the calculations and make the necessary adjustments described under paragraph (f)(2)(viii) of this section if, and only if, PRS has—

(*1*) An excess business interest expense greater than $0 under paragraph (f)(2)(i) of this section;

(*2*) A total negative allocable ATI greater than $0 under paragraph (f)(2)(vi) of this section; and

(*3*) A total ATIC excess amount greater than $0 under paragraph (f)(2)(vii) of this section. Because PRS satisfies each of these three requirements, PRS must perform the calculations and make the necessary adjustments described under paragraph (f)(2)(viii) of this section.

(B) PRS must determine each partner's priority amount and usable priority amount. Only partners with an ATIC deficit under paragraph (f)(2)(vii) of this section of this section can have a priority amount greater than $0. Thus, only partners B, C, and D can have a priority amount greater than $0. PRS determines a partner's priority amount as 30 percent of the amount by which such partner's allocable positive ATI exceeds its final allocable ATI. Therefore, B's priority amount is $9 (($50 − $20) × 30 percent), C's priority amount is $72 (($400 − $160) × 30 percent), and D's priority amount is $0 (($0 − $0) × 30 percent). Thus, the total priority amount is $81 ($0 + $9 + $72 + $0). Next, PRS must determine each partner's usable priority amount. Each partner's usable priority amount is the lesser of such partner's priority amount or ATIC deficit. Thus, B has a usable priority amount of $9, C has a usable priority amount of $2, and D has a usable priority amount of $0. As a result, the total usable priority amount is $11 ($0 + $9 + $2 + $0). Because the total usable priority amount ($11) is greater than the total ATIC excess ($6) under paragraph (f)(2)(vii) of this section, PRS must perform the adjustments described in paragraph (f)(2)(viii)(D) of this section.

TABLE 53 TO PARAGRAPH (o)(21)(viii)(B)

	A	B	C	D	Total
(Positive allocable ATI − Final allocable ATI)	$0	$30	$240	$0	N/A
Multiplied by 30 percent	30%	30%	30%	30%	N/A
= Priority amount	$0	$9	$72	$0	$81

TABLE 54 TO PARAGRAPH (o)(21)(viii)(B)

	A	B	C	D	Total
Priority amount	$0	$9	$72	$0	N/A
ATIC deficit	0	44	2	50	N/A
Lesser of priority amount or ATIC deficit = Usable priority amount	0	9	2	0	$11

(C) In light of the fact that the total usable priority amount is greater than the total ATIC excess under paragraph (f)(2)(viii)(B) of this section, paragraph (f)(2)(viii)(C) of this section does not apply.

(D)(*1*) Because B and C are the only partners with priority amounts greater than $0, B and C are priority partners, while A and D are non-priority partners. For purposes of paragraph (f)(2)(ix) of this section, each partner's final ATIC excess amount is $0. For purposes of paragraph (f)(2)(x) of this section, each non-priority partner's final ATIC deficit amount is such partner's ATIC deficit determined pursuant to paragraph (f)(2)(vii) of this section. Therefore, A has a final ATIC deficit of $0 and D has a final ATIC deficit of $50. Additionally, for purposes of paragraph (f)(2)(x) of this section, PRS must determine each priority partner's step eight excess share. A priority partner's step eight excess share is the product of the total ATIC excess and the ratio of the partner's priority amount to the total priority amount. Thus, B's step eight excess share is $0.67 ($6 × ($9/$81)) and C's step eight excess share is $5.33 ($6 × ($72/$81)). To the extent a priority partner's step eight excess share exceeds its ATIC deficit, the excess will be the partner's ATIC excess for purposes of paragraph (f)(2)(x) of this section. B's step eight excess share does not exceed its ATIC deficit. Because C's step eight excess share ($5.33) exceeds its ATIC deficit ($2), C's ATIC excess for purposes of paragraph (f)(2)(x) of this section is $3.33 ($5.33 − $2). Thus, the total ATIC excess for purposes of paragraph (f)(2)(x) of this section is $3.33 ($0 + $3.33). To the extent a priority partner's ATIC deficit exceeds its step eight excess share, the excess will be the partner's ATIC deficit for purposes of paragraph (f)(2)(x) of this section. Because B's ATIC deficit ($44) exceeds its step eight excess share ($0.67), B's ATIC deficit for purposes of paragraph (f)(2)(x) of this section is $43.33 ($44 − $0.67). C's ATIC deficit does not exceed its step eight excess share. Thus, the total ATIC deficit for purposes of paragraph (f)(2)(x) of this section is $43.33 ($43.33 + $0).

TABLE 55 TO PARAGRAPH (o)(21)(viii)(D)(1)

	A	B	C	D	Total
Non-priority partners ATIC deficit in paragraph (f)(2)(vii) = Final ATIC deficit for purposes of paragraph (f)(2)(x) of this section	$0	N/A	N/A	$50	N/A

TABLE 56 TO PARAGRAPH (o)(21)(viii)(D)(1)

	A	B	C	D	Total
Priority partners step eight excess share = (Total ATIC excess) × (Priority/Total priority)	N/A	$0.67	$5.33	N/A	N/A
ATIC deficit	N/A	44	2	N/A	N/A
If step eight excess share exceeds ATIC deficit, then such excess = ATIC excess for purposes of paragraph (f)(2)(x) of this section	N/A	0	3.33	N/A	$3.33
If ATIC deficit exceeds step eight excess share, then such excess = ATIC deficit for purposes of paragraph (f)(2)(x) of this section	N/A	43.33	0	N/A	43.33

(*2*) In sum, the correct amounts to be used in paragraphs (o)(21)(ix) and (x) of this section are as follows.

TABLE 57 TO PARAGRAPH (o)(21)(viii)(D)(2)

	A	B	C	D	Total
ATIC excess	$0	$0	$3.33	$0	$3.33
ATIC deficit	0	43.33	0	0	43.33
Non-priority partner final ATIC deficit	0	0	0	50	N/A

(ix) Ninth, PRS determines each partner's final ATIC excess amount. Pursuant to paragraph (f)(2)(viii)(D) of this section, each priority and non-priority partner's final ATIC excess amount is $0.

(x) Tenth, PRS determines each partner's final ATIC deficit amount. Because B has an ATIC deficit, PRS must determine B's final ATIC deficit amount. B's final ATIC deficit amount is B's ATIC deficit ($43.33), reduced, but not below $0, by the product of the total ATIC excess ($3.33) and the ratio of B's ATIC deficit to the total ATIC deficit ($43.33/$43.33). Therefore, B has $40 of final ATIC deficit ($43.33 − ($3.33 × 100 percent)). Pursuant to paragraph (f)(2)(viii)(D) of this section, D's final ATIC deficit amount is $40.

TABLE 58 TO PARAGRAPH (o)(21)(x)

	A	B	C	D	Total
ATIC deficit	$0	$43.33	$0	N/A	N/A

TABLE 58 TO PARAGRAPH (o)(21)(x)—Continued

	A	B	C	D	Total
Less: (Total ATIC excess) × (ATIC deficit/Total ATIC deficit)	0	3.33	0	N/A	N/A
= Final ATIC deficit	0	40	0	$50	$90

(xi) Eleventh, PRS allocates deductible business interest expense and section 163(j) excess items to the partners. Pursuant to paragraph (f)(2)(i) of this section, PRS has $90 of excess business interest expense. PRS allocates the excess business interest expense dollar for dollar to the partners with final ATIC deficits. Thus, PRS allocates its excess business interest expense $40 to B and $50 to D. A partner's allocable business interest expense is deductible business interest expense to the extent it exceeds such partner's share of excess business interest expense. Therefore, A has deductible business interest expense of $0 ($0 − $0), B has deductible business interest expense of $10 ($50 − $40), C has deductible business interest expense of $50 ($50 − $0), and D has deductible business interest expense of $0 ($50 − $50).

TABLE 59 TO PARAGRAPH (o)(21)(xi)

	A	B	C	D	Total
Deductible BIE	$0	$10	$50	$0	$60
EBIE allocated	0	40	0	50	90
ETI allocated	0	0	0	0	0
EBII allocated	0	0	0	0	0

(22) *Example 22*—(i) *Facts.* A and B are equal shareholders in X, a subchapter S corporation. In Year 1, X has $100 of ATI and $40 of business interest expense. A has $100 of ATI and $20 of business interest expense from its sole proprietorship. B has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *S corporation-level.* In Year 1, X's section 163(j) limit is 30 percent of its ATI, or $30 ($100 × 30 percent). Thus, X has $30 of deductible business interest expense and $10 of disallowed business interest expense. Such $30 of deductible business interest expense is includable in X's nonseparately stated income or loss, and is not subject to further limitation under section 163(j). X carries forward the $10 of disallowed business interest expense to Year 2 as a disallowed business interest expense carryforward under § 1.163(j)–2(c). X may not currently deduct all $40 of its business interest expense in Year 1. X only reduces its accumulated adjustments account in Year 1 by the $30 of deductible business interest expense in Year 1 under § 1.163(j)–6(l)(7).

(iii) *Shareholder allocations.* A and B are each allocated $35 of nonseparately stated taxable income ($50 items of income or gain, less $15 of deductible business interest expense) from X. A and B do not reduce their basis in X by the $10 of disallowed business interest expense.

(iv) *Shareholder-level computations.* A, in computing its limit under section 163(j), has $100 of ATI and $20 of business interest expense from its sole proprietorship. A's section 163(j) limit is $30 ($100 × 30 percent). Thus, A's $20 of business interest expense is deductible business interest expense. B, in computing its limit under section 163(j), has $20 of business interest expense from its sole proprietorship. B's section 163(j) limit is $0 ($0 × 30 percent). Thus, B's $20 of business interest expense is not allowed as a deduction and is treated as business interest expense paid or accrued by B in Year 2.

(23) *Example 23*—(i) *Facts.* The facts are the same as in *Example 22* in paragraph (o)(22)(i) of this section. In Year 2, X has $233.33 of ATI, $0 of business interest income, and $30 of business interest expense. A has $100 of ATI and $20 of business interest expense from its sole proprietorship. B has $0 of ATI and $20 of business interest expense from its sole proprietorship.

(ii) *S corporation-level.* In Year 2, X's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $70 ($233.33 × 30 percent). Because X's section 163(j) limit exceeds X's $40 of business interest expense ($30 from Year 2, plus the $10 disallowed business interest expense carryforwards from Year 1), X may deduct all $40 of business interest expense in Year 2. Such $40 of deductible business interest expense is includable in X's nonseparately stated income or loss, and is not subject to further limitation under section 163(j). Pursuant to § 1.163(j)–6(l)(7), X must reduce its accumulated adjustments account by $40. Additionally, X has $100 of excess taxable income under § 1.163(j)–1(b)(17).

(iii) *Shareholder allocations.* A and B are each allocated $96.67 of nonseparately stated taxable income ($116.67 items of income or gain, less $20 of deductible business interest expense) from X. Additionally, A and B are each allocated $50 of excess taxable income under § 1.163(j)–6(l)(4). As a result, A and B each increase their ATI by $50.

(iv) *Shareholder-level computations.* A, in computing its limit under section 163(j), has $150 of ATI ($100 from its sole proprietorship, plus $50 excess taxable income) and $20 of business interest expense (from its sole proprietorship). A's section 163(j) limit is $45 ($150 × 30 percent). Thus, A's $20 of business interest expense is deductible business interest expense. B, in computing its limit under section 163(j), has $50 of ATI ($0 from its sole proprietorship, plus $50 excess taxable income) and $40 of business interest expense ($20 from its sole proprietorship, plus $20 disallowed business interest expense from its sole proprietorship in Year 1). B's section 163(j) limit is $15 ($50 × 30 percent). Thus, $15 of B's business interest expense is deductible business interest expense. The $25 of B's business interest expense not allowed as a deduction ($40 business interest expense, less $15 section 163(j) limit) is treated as business interest expense paid or accrued by B in Year 3.

(p) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

§ 1.163(j)–7 Application of the section 163(j) limitation to foreign corporations and United States shareholders.

(a) *Overview.* This section provides rules for the application of section 163(j) to relevant foreign corporations with shareholders that are United States persons. Paragraph (b) of this section describes the general rule regarding the application of section 163(j) to relevant foreign corporations. Paragraphs (c) through (f) of this section are reserved. Paragraph (g) of this section provides rules concerning the computation of ATI of a relevant foreign corporation. Paragraphs (h) through (k) of this section are reserved.

(b) *General rule regarding the application of section 163(j) to relevant foreign corporations.* Except as otherwise provided in this section, section 163(j) and the section 163(j) regulations apply to determine the deductibility of a relevant foreign corporation's business interest expense for purposes of computing its taxable income for U.S. income tax purposes (if any) in the same manner as those provisions apply to determine the deductibility of a domestic C corporation's business interest expense for purposes of computing its taxable income. See also § 1.952–2. If a relevant foreign corporation is a direct or indirect partner in a partnership, see § 1.163(j)–6 (concerning the application of section 163(j) to partnerships).

(c)–(f) [Reserved]

(g) *Rules concerning the computation of adjusted taxable income of a relevant foreign corporation*—(1) *Tentative taxable income.* For purposes of computing the tentative taxable income of a relevant foreign corporation for a taxable year, the relevant foreign corporation's gross income and allowable deductions are determined under the principles of § 1.952–2 or under the rules of section 882 for determining income that is, or deductions that are allocable to, effectively connected income, as applicable.

(2) *Treatment of certain dividends.* For purposes of computing the ATI of a relevant foreign corporation for a taxable year, any dividend included in gross income that is received from a related person, within the meaning of section 954(d)(3), with respect to the distributee is subtracted from tentative taxable income.

(h)–(l) [Reserved]

(m) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

§ 1.163(j)–8. [Reserved]

§ 1.163(j)–9 Elections for excepted trades or businesses; safe harbor for certain REITs.

(a) *Overview.* The limitation in section 163(j) applies to business interest, which is defined under section 163(j)(5) as interest properly allocable to a trade or business. The term trade or business does not include any electing real property trade or business or any electing farming business. See section 163(j)(7). This section provides the rules and procedures for taxpayers to follow in making an election under section 163(j)(7)(B) for a trade or business to be an electing real property trade or business and an election under section 163(j)(7)(C) for a trade or business to be an electing farming business.

(b) *Availability of election*—(1) *In general.* An election under section 163(j)(7)(B) for a real property trade or business to be an electing real property trade or business is available to any trade or business that is described in § 1.163(j)–1(b)(14)(i), (ii), or (iii), and an election under section 163(j)(7)(C) for a farming business to be an electing farming business is available to any trade or business that is described in § 1.163(j)–1(b)(13)(i), (ii), or (iii).

(2) *Special rules*—(i) *Exempt small businesses.* An election described in paragraph (b)(1) of this section is available regardless of whether the real property trade or business or farming business making the election also meets the requirements of the small business exemption in section 163(j)(3) and § 1.163(j)–2(d). See paragraph (c)(2) of this section for the effect of the election relating to depreciation.

(ii) *Section 162 trade or business not required for electing real property trade or business.* An election described in paragraph (b)(1) of this section to be an electing real property trade or business is available regardless of whether the trade or business with respect to which the election is made is a trade or business under section 162. For example, a taxpayer engaged in activities described in section 469(c)(7)(C) and § 1.469–9(b)(2), as required in § 1.163(j)–1(b)(14)(i), may make an election for a trade or business to be an electing real property trade or business, regardless of whether its activities rise to the level of a section 162 trade or business.

(c) *Scope and effect of election*—(1) *In general.* An election under this section is made with respect to each eligible trade or business of the taxpayer and applies only to such trade or business for which the election is made. An election under this section applies to the taxable year in which the election is made and to all subsequent taxable years. See paragraph (e) of this section for terminations of elections.

(2) *Irrevocability.* An election under this section is irrevocable.

(3) *Depreciation.* Taxpayers making an election under this section are required to use the alternative depreciation system for certain types of property under section 163(j)(11) and cannot claim the additional first-year depreciation deduction under section 168(k) for those types of property.

(d) *Time and manner of making election*—(1) *In general.* Subject to paragraph (f) of this section, a taxpayer makes an election under this section by attaching an election statement to the taxpayer's timely filed original Federal income tax return, including extensions. A taxpayer may make elections for multiple trades or businesses on a single election statement.

(2) *Election statement contents.* The election statement should be titled ''Section 1.163(j)–9 Election'' and must contain the following information for each trade or business:

(i) The taxpayer's name;

(ii) The taxpayer's address;

(iii) The taxpayer's social security number (SSN) or employer identification number (EIN);

(iv) A description of the taxpayer's electing trade or business sufficient to demonstrate qualification for an election under this section, including the principal business activity code; and

(v) A statement that the taxpayer is making an election under section 163(j)(7)(B) or (C), as applicable.

(3) *Consolidated group's trade or business.* For a consolidated group's trade or business, the election under this section is made by the agent for the group, as defined in § 1.1502–77, on behalf of itself and members of the consolidated group. Only the name and taxpayer identification number (TIN) of the agent for the group, as defined in § 1.1502–77, must be provided on the election statement.

(4) *Partnership's trade or business.* An election for a partnership must be made on the partnership's return for a trade or business that the partnership conducts. An election by a partnership does not apply to a trade or business conducted by a partner outside the partnership.

(e) *Termination of election*—(1) *In general.* An election under this section automatically terminates if a taxpayer ceases to engage in the electing trade or business. A taxpayer is considered to cease to engage in an electing trade or business if the taxpayer sells or transfers substantially all of the assets of the electing trade or business to an acquirer that is not a related party in a taxable asset transfer. A taxpayer is also considered to cease to engage in an electing trade or business if the taxpayer terminates its existence for Federal income tax purposes or ceases operation of the electing trade or business, except to the extent that such termination or cessation results in the sale or transfer of substantially all of the assets of the electing trade or business to an acquirer that is a related party, or in a transaction that is not a taxable asset transfer.

(2) *Taxable asset transfer defined.* For purposes of this paragraph (e), the term *taxable asset transfer* means a transfer in which the acquirer's basis or adjusted basis in the assets is not determined, directly or indirectly, in whole or in part, by reference to the transferor's basis in the assets.

(3) *Related party defined.* For purposes of this paragraph (e), the term *related party* means any person who bears a relationship to the taxpayer which is described in section 267(b) or 707(b)(1).

(4) *Anti-abuse rule.* If, within 60 months of a sale or transfer of assets described in paragraph (e)(1) of this section, the taxpayer or a related party reacquires substantially all of the assets that were used in the taxpayer's prior electing trade or business, or substantially similar assets, and resumes conducting such prior electing trade or business, the taxpayer's previously terminated election under this section is reinstated and is effective on the date the prior electing trade or business is reacquired.

(f) *Additional guidance.* The rules and procedures regarding the time and manner of making an election under this section and the election statement contents in paragraph (d) of this section may be modified through other guidance (see §§ 601.601(d) and 601.602 of this chapter). Additional situations in which an election may terminate under paragraph (e) of this section may be provided through guidance published in the **Federal Register** or in the Internal Revenue Bulletin (see § 601.601(d) of this chapter).

(g) *Examples.* The examples in this paragraph (g) illustrate the application of this section. Unless otherwise indicated, X and Y are domestic C corporations; D and E are U.S. resident individuals not subject to any foreign income tax; and the exemption for certain small businesses in § 1.163(j)–2(d) does not apply.

(1) *Example 1: Scope of election*—(i) *Facts.* For the taxable year ending December 31, 2021, D, a sole proprietor, owned and operated a dairy farm and an orchard as separate farming businesses described in section 263A(e)(4). D filed an original Federal income tax return for the 2021 taxable year on August 1, 2022, and included with the return an election statement meeting the requirements of paragraph (d)(2) of this section. The election statement identified D's dairy farm business as an electing trade or business under this section. On March 1, 2023, D sold some but not all or substantially all of the assets from D's dairy farm business to D's neighbor, E, who is unrelated to D. After the sale, D continued to operate the dairy farm trade or business.

(ii) *Analysis.* D's election under this section was properly made and is effective for the 2021 taxable year and subsequent years. D's dairy farm business is an excepted trade or business because D made the election with D's timely filed Federal income tax return. D's orchard business is a non-excepted trade or business, because D did not make an election for the orchard business to be an excepted trade or business. The sale of some but not all or substantially all of the assets from D's dairy farm business does not affect D's election under this section.

(2) *Example 2: Availability of election*—(i) *Facts.* E, an individual, operates a dairy business that is a farming business under section 263A and also owns real property that is not part of E's dairy business that E leases to an unrelated party through a triple net lease. E's average gross receipts, excluding inherently personal amounts, for the three years prior to 2021 are approximately $25 million, but E is unsure of the exact amount.

(ii) *Analysis.* Under paragraph (b)(2)(i) of this section, E may make an election under this section for the dairy business to be an electing farming business, even though E is unsure whether the small business exemption of § 1.163(j)–2(d) applies. Additionally, under paragraph (b)(2)(ii) of this section, assuming the requirements of section 163(j)(7)(C) and this section are otherwise satisfied, E may make an election under this section for its triple net lease property to be an electing real property trade or business, even though E may not be engaged in a trade or business under section 162 with respect to the real property.

(3) *Example 3: Cessation of entire trade or business*—(i) *Facts.* X has a real property trade or business for which X made an election under this section by attaching an election statement to A's 2021 Federal income tax return. On March 1, 2022, X sold all of the assets used in its real property trade or business to Y, an unrelated party, and ceased to engage in the electing trade or business. On June 1, 2027, X started a new real property trade or business that was substantially similar to X's prior electing trade or business.

(ii) *Analysis.* X's election under this section terminated on March 1, 2022, under paragraph (e)(1) of this section. X may choose whether to make an election under this section for X's new real property trade or business that A started in 2027.

(4) *Example 4: Anti-abuse rule*—(i) *Facts.* The facts are the same as in *Example 3* in paragraph (g)(3)(i) of this section, except that X re-started its previous real property trade or business on February 1, 2023, when X reacquired substantially all of the assets that X had sold on March 1, 2022.

(ii) *Analysis.* X's election under this section terminated on March, 1, 2022, under paragraph (e)(1) of this section. On February 1, 2023, X's election was reinstated under paragraph (e)(4) of this section. X's new real property trade or business is treated as a resumption of X's prior electing trade or business and is therefore treated as an electing real property trade or business.

(5) *Example 5: Trade or business continuing after acquisition*—(i) *Facts.* X has a farming business for which X made an election under this section by attaching an election statement to X's timely filed 2021 Federal income tax return. Y, unrelated to X, also has a farming business, but Y has not made an election under this section. On July 1, 2022, X transferred all of its assets to Y in a transaction described in section 368(a)(1)(D). After the transfer, Y continues to operate the farming trade or business acquired from X.

(ii) *Analysis.* Under paragraph (e)(1) of this section, Y is subject to X's election under this section for the trade or business that uses X's assets because the sale or transfer was not in a taxable transaction. Y cannot revoke X's election, but X's election has no effect on Y's existing farming business for which Y has not made an election under this section.

(6) *Example 6: Trade or business merged after acquisition*—(i) *Facts.* The facts are the same as in *Example 5* in paragraph (g)(5)(i) of this section, except that Y uses the assets acquired from X in a trade or business that is neither a farming business (as defined in section 263A(e)(4) or § 1.263A–4(a)(4)) nor a trade or business of a specified agricultural or horticultural cooperative (as defined in section 199A(g)(4)).

(ii) *Analysis.* Y is not subject to X's election for Y's farming business because the farming trade or business ceased to exist after the acquisition.

(h) *Safe harbor for REITs*—(1) *In general.* If a REIT holds real property, as defined in § 1.856–10, interests in one or more partnerships directly or indirectly holding real property (through interests in other partnerships or shares in other REITs), as defined in § 1.856–10, or shares in one or more other REITs directly or indirectly holding real property (through interests in partnerships or shares in other REITs), as defined in § 1.856–10, the REIT is eligible to make the election described in paragraph (b)(1) of this section to be an electing real property trade or business for purposes of sections 163(j)(7)(B) and 168(g)(1)(F) for all or part of its assets. The portion of the REIT's assets eligible for this election is determined under paragraph (h)(2) or (3) of this section.

(2) *REITs that do not significantly invest in real property financing assets.* If a REIT makes the election under paragraph (h)(1) of this section and the value of the REIT's real property financing assets, as defined in paragraphs (h)(5) and (6) of this section, at the close of the taxable year is 10 percent or less of the value of the REIT's total assets at the close of the taxable year, as determined under section 856(c)(4)(A), then all of the REIT's assets are treated as assets of an excepted trade or business.

(3) *REITs that significantly invest in real property financing assets.* If a REIT makes the election under paragraph (h)(1) of this section and the value of the REIT's real property financing assets, as defined in paragraphs (h)(5) and (6) of this section, at the close of the taxable year is more than 10 percent of the value of the REIT's total assets at the close of the taxable year, as determined under section 856(c)(4)(A), then for the allocation of interest expense, interest income, and other items of expense and gross income to excepted and non-excepted trades or businesses, the REIT must apply the rules set forth in § 1.163(j)–10 as modified by paragraph (h)(4) of this section.

(4) *REIT real property assets, interests in partnerships, and shares in other REITs*—(i) *Real property assets.* Assets held by a REIT described in paragraph (h)(3) of this section that meet the definition of real property under § 1.856–10 are treated as assets of an excepted trade or business.

(ii) *Partnership interests.* If a REIT described in paragraph (h)(3) of this section holds an interest in a partnership, in applying the partnership look-through rule described in § 1.163(j)–10(c)(5)(ii)(A)(*2*), the REIT treats assets of the partnership that meet the definition of real property under § 1.856–10 as assets of an excepted trade or business. This application of the definition of real property under § 1.856–10 does not affect the characterization of the partnership's assets at the partnership level or for any non-REIT partner. However, no portion of the adjusted basis of the REIT's interest in the partnership is allocated to a non-excepted trade or business if the partnership makes an election under paragraph (h)(7) of this section and if all of the partnership's assets are treated as assets of an excepted trade or business under paragraph (h)(2) of this section.

(iii) *Shares in other REITs*—(A) *In general.* If a REIT (shareholder REIT) described in paragraph (h)(3) of this section holds an interest in another REIT, then for purposes of applying the allocation rules in § 1.163(j)–10, the partnership look-through rule described in § 1.163(j)–10(c)(5)(ii)(A)(*2*), as modified by paragraph (h)(4)(ii) of this section, applies to the assets of the other REIT (as if the other REIT were a partnership) in determining the portion of shareholder REIT's adjusted basis in the shares of the other REIT that is allocable to an excepted or non-excepted trade or business of shareholder REIT. However, no portion of the adjusted basis of shareholder REIT's shares in the other REIT is allocated to a non-excepted trade or business if all of the other REIT's assets are treated as assets of an excepted trade or business under paragraph (h)(2) of this section.

(B) *Information necessary.* If shareholder REIT does not receive, either directly from the other REIT or indirectly through the analysis of an applicable financial statement (within the meaning of section 451(b)(3)) of the other REIT, the information necessary to determine whether and to what extent the assets of the other REIT are investments in real property financing assets, then shareholder REIT's shares in the other REIT are treated as assets of a non-excepted trade or business under § 1.163(j)–10(c).

(iv) *Tiered entities.* In applying § 1.163(j)–10(c)(5)(ii)(E), the rules in paragraphs (h)(4)(ii) and (h)(4)(iii)(A) and (B) of this section apply to any partnerships and other REITs within the tier.

(5) *Value of shares in other REITs*—(i) *In general.* If a REIT (shareholder REIT) holds shares in another REIT, then solely for purposes of applying the value tests under paragraphs (h)(2) and (3) of this section, the value of shareholder REIT's real property financing assets includes the portion of the value of shareholder REIT's shares in the other REIT that is attributable to the other REIT's investments in real property financing assets. However, no portion of the value of shareholder REIT's shares in the other REIT is included in the value of shareholder REIT's real property financing assets if all of the other REIT's assets are treated as assets of an excepted trade or business under paragraph (h)(2) of this section.

(ii) *Information necessary.* If shareholder REIT does not receive, either directly from the other REIT or indirectly through the analysis of an applicable financial statement (within the meaning of section 451(b)(3)) of the other REIT, the information necessary to determine whether and to what extent the assets of the other REIT are investments in real property financing assets, then shareholder REIT's shares in the other REIT are treated as real property financing assets for purposes of paragraphs (h)(2) and (3) of this section.

(iii) *Tiered REITs.* The rules in paragraphs (h)(5)(i) and (ii) of this section apply successively to the extent that the other REIT, and any other REIT in the tier, holds shares in another REIT.

(6) *Real property financing assets.* For purposes of this paragraph (h), *real property financing assets* include interests, including participation interests, in the following: Mortgages, deeds of trust, and installment land contracts; mortgage pass-through certificates guaranteed by Government National Mortgage Association (GNMA), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), or Canada Mortgage and Housing Corporation (CMHC); REMIC regular interests; other interests in investment trusts classified as trusts under § 301.7701–4(c) of this chapter that represent undivided beneficial ownership in a pool of obligations principally secured by interests in real property and related assets that would be permitted investments if the investment trust were a REMIC; obligations secured by manufactured housing treated as single family residences under section 25(e)(10), without regard to the treatment of the obligations or the properties under state law; and debt instruments issued by publicly offered REITs.

(7) *Application of safe harbor for partnerships controlled by REITs.* A partnership is eligible to make the election under paragraph (h)(1) of this section if one or more REITs own directly or indirectly at least 50 percent of the partnership's capital and profits, the partnership meets the requirements of section 856(c)(2), (3), and (4) as if the partnership were a REIT, and the partnership satisfies the requirements described in paragraph (h)(1) of this section as if the partnership were a REIT. The portion of the partnership's assets eligible for this election is determined under paragraph (h)(2) or (3) of this section, treating the partnership as if it were a REIT.

(8) *REITs or partnerships controlled by REITs that do not apply the safe harbor.* A REIT or a partnership that is eligible but chooses not to apply the safe harbor provisions of paragraph (h)(1) or (7) of this section, respectively, may still elect, under paragraph (b)(1) of this section, for one or more of its trades or businesses to be an electing real property trade or business, provided that such trade or business is otherwise eligible to elect under paragraph (b)(1) of this section. A REIT or partnership that makes the election under paragraph (b)(1) of this section without utilizing the safe harbor provisions of paragraph (h) of this section may not rely on any portion of paragraphs (h)(1) through (7) of this section.

(i) [Reserved]

(j) *Special anti-abuse rule for certain real property trades or businesses*—(1) *In general.* Except as provided in paragraph (j)(2) of this section, a trade or business (lessor) does not constitute a trade or business eligible for an election described in paragraph (b)(1) of this section to be an electing real property trade or business if at least 80 percent, determined by fair market rental value, of the real property used in the business is leased to a trade or business (lessee) under common control with the lessor, regardless of whether the arrangement is pursuant to a written lease or pursuant to a service contract or another agreement that is not denominated as a lease. For purposes of this paragraph (j), fair market rental value is the amount of rent that a prospective lessee that is unrelated to the lessor would be willing to pay for a rental interest in real property, taking into account the geographic location, size, and type of the real property. For purposes of this paragraph (j), two trades or businesses are under common control if 50 percent of the direct and indirect ownership of both businesses are held by related parties within the meaning of sections 267(b) and 707(b).

(2) *Exceptions*—(i) *De minimis exception.* The limitation in paragraph (j)(1) of this section does not apply, and the lessor is eligible to make an election under paragraph (b)(1) of this section, if the lessor leases, regardless of whether the arrangement is pursuant to a written lease or pursuant to a service contract or another agreement that is not denominated as a lease, at least 90 percent of the lessor's real property, determined by fair market rental value, to one or more of the following:

(A) A party not under common control with the lessor or lessee;

(B) A party under common control with the lessor or lessee that has made an election described in paragraph (b)(1) of this section for a trade or business to be an electing real property trade or business or electing farming business, but only to the extent that the real property is used as part of its electing real property trade or business or electing farming business; or

(C) A party under common control with the lessor or lessee that is an excepted regulated utility trade or business, but only to the extent that the real property is used as part of its excepted regulated utility trade or business.

(ii) *Look-through exception.* If the de minimis exception in paragraph (j)(2)(i) of this section does not apply because less than 90 percent of the lessor's real property is leased to parties described in paragraphs (j)(2)(i)(A), (B), and (C), the lessor is eligible to make the election under paragraph (b)(1) of this section to the extent that the lessor leases the real property to parties described in paragraph (j)(2)(A), (B), or (C), and to the extent that the lessee subleases (or lessees ultimately sublease) the real property to:

(A) A party not under common control with the lessor or lessee;

(B) A party under common control with the lessor or lessee that has made an election described in paragraph (b)(1) of this section for a trade or business to be an electing real property trade or business or electing farming business to the extent that the real property is used as part of its electing real property trade or business or electing farming business; or

(C) A party under common control with the lessor or lessee that is an excepted regulated utility trade or business to the extent that the real property is used as part of its excepted regulated utility trade or business.

(iii) *Inapplicability of exceptions to consolidated groups.* The exceptions in paragraphs (j)(2)(i) and (ii) of this section do not apply when the lessor and lessee are members of the same consolidated group.

(iv) *Exception for certain REITs.* The special anti-abuse rule in paragraph (j)(1) of this section does not apply to REITs or to partnerships making an election under paragraph (h)(7) of this section that lease qualified lodging facilities, as defined in section 856(d)(9)(D), and qualified health care properties, as defined in section 856(e)(6)(D).

(3) *Allocations.* See § 1.163(j)–10(c)(3)(iii)(D) for rules related to the allocation of the basis of assets used in lessor trades or businesses described in paragraphs (j)(1) and (j)(2)(i) of this section.

(4) *Examples.* The examples in this paragraph (j)(4) illustrate the application of paragraphs (j)(1), (2), and (3) of this section. Unless otherwise indicated, the parties are all domestic entities and are not members of a single consolidated group within the meaning of § 1.1502–1(h).

(i) *Example 1: Related party lease of hotel*—(A) *Facts.* X and Y are under common control, as defined in paragraph (j)(1) of this section. X owns one piece of real property, a hotel, that X leases to Y. Y operates the hotel and provides hotel rooms and associated amenities to third party guests of the hotel. The form of the arrangement with third party hotel guests is a license to use rooms in the hotel and associated amenities. Y is a real property trade or business that has made an election under paragraph (b)(1) of this section.

(B) *Analysis.* Because X leases at least 80 percent of X's real property to a party under common control, X is subject to the anti-abuse rule in paragraph (j)(1) of this section. However, under the de minimis exception under paragraph (j)(2)(i) of this section, 100 percent of the fair market rental value of the building is leased to a party under common control that has made an election to be an electing real property trade or business. Accordingly, X is eligible to make the election described in paragraph (b)(1) of this section for its entire trade or business.

(ii) *Example 2*—(A) *Facts.* The facts are the same as in *Example 1* in paragraph (j)(4)(i)(A) of this section, except that Y has not made an election under paragraph (b)(1) of this section, and is not otherwise using the real property in an excepted trade or business.

(B) *Analysis.* Because X leases at least 80 percent of X's real property, determined by fair market rental value, to Y, a party under common control, X is subject to the anti-abuse rule in paragraph (j)(1) of this section. X is not eligible for the de minimis exception under paragraph (j)(2)(i) of this section because X does not lease at least 90 percent of its real property to a party under common control, as defined in paragraph (j)(1) of this section, such as Y, and Y is not using the property in an otherwise excepted trade or business. However, X is eligible for the look-through exception under paragraph (j)(2)(ii) of this section because X leases 100 percent of its real property to Y, a party that is under common control, and Y subleases 100 percent of the real property to parties that are not under common control with X or Y. The fact that the license provided to hotel guests is not denominated as a lease does not prevent these licenses from being treated as a lease for purposes of paragraph (j) of this section. Accordingly, under the look-through exception under paragraph (j)(2)(ii) of this section, X is eligible to make the election described in paragraph (b)(1) of this section with regard to its entire trade or business.

(iii) *Example 3: Sublease to related party and unrelated third party*—(A) *Facts.* X owns one piece of real property that X leases to Y, a party under common control, as defined in paragraph (j)(1) of this section. Y does not operate an excepted trade or business. Y subleases 80 percent of the real property, determined by the fair market rental value, to a party under common control with Y that does not operate an excepted trade or business and 20 percent of the real property, determined by the fair market rental value, to an unrelated third party.

(B) *Analysis.* Because X leases at least 80 percent of X's real property, determined by fair market rental value, to a party under common control, X is subject to the anti-abuse rule in paragraph (j)(1) of this section. X is not eligible for the de minimis exception in paragraph (j)(2)(i) of this section because X is not leasing at least 90 percent of the real property, determined by fair market rental value, to a party under common control that operates an excepted trade or business and/or unrelated parties. Under the look-through exception under paragraph (j)(2)(ii) of this section, X is eligible to make the election described in paragraph (b)(1) of this section with respect to the 20 percent of the fair market rental value of the real property subleased to an unrelated party because X is treated as directly leasing this portion to an unrelated party. X is not eligible to make the election described in paragraph (b)(1) of this section with respect to the 80 percent of the building subleased to a party under common control because X is still treated as directly leasing this portion to a related party. Under § 1.163(j)–10(c)(3)(iii)(D), X must allocate 80 percent of the basis in the real property as a non-excepted trade or business and 20 percent of the basis in the real property as an excepted trade or business.

(iv) *Example 4: Multiple subleases*—(A) *Facts.* X owns a building that X leases to Y, a party under common control as defined in paragraph (j)(1) of this section. Y does not operate an excepted trade or business. Y subleases 80 percent of the building, determined by fair market rental value, to Z, a party under common control with both X and Y. Y subleases the remaining 20 percent of the building, determined by fair market rental value, to unrelated parties. Z subleases 50 percent of its leasehold interest, determined by fair market rental value, to parties unrelated to X, Y and Z, and uses the remaining leasehold interest in its retail business. Z does not operate an excepted trade or business.

(B) *Analysis.* Because X leases at least 80 percent of X's real property, determined by fair market rental value, to a party under common control, X is subject to the anti-abuse rule in paragraph (j)(1) of this section. X is not eligible for the de minimis exception in paragraph (j)(2)(i) because X is not leasing at least 90 percent of the building, determined by fair market rental value, to a party under common control that operates an excepted trade or business and/or unrelated parties. Under the look-through exception under paragraph (j)(2)(ii) of this section, X is eligible to make the election described in paragraph (b)(1) of this section with respect to the 60 percent of the building that is subleased to unrelated parties, determined by adding 40 percent (50 percent of the 80 percent leasehold interest) from Z's sublease to an unrelated party and 20 percent from Y's sublease to unrelated parties (40 + 20). X is not eligible to make the election described in paragraph (b)(1) of this section with respect to the 40 percent of the building subleased to Z, because Z is a related party that does not operate an excepted trade or business.

(v) *Example 5: Lessee's Trade or Business*—(A) *Facts.* X owns a building that X leases to W, a party under common control as defined in paragraph (j)(1) of this section. W operates the building as a widget manufacturing plant and does not sublease any portion of the building.

(B) *Analysis.* X is not eligible to make the election described in paragraph (b)(1) of this section because X leases the entire building to a party under common control. X is not eligible for the de minimis exception in paragraph (j)(2)(i) of this section because X is not leasing at least 90 percent of the real property to a party under common control that operates an excepted trade or business and/or unrelated parties. W's trade or business cannot be an electing real property trade or business. X is not eligible for the look-through exception under paragraph (j)(2)(ii) of this section because W is not subleasing any part of the building.

(k) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

§ 1.163(j)–10 Allocation of interest expense, interest income, and other items of expense and gross income to an excepted trade or business.

(a) *Overview*—(1) *In general*—(i) *Purposes.* Except as provided in § 1.163(j)–6(m) or § 1.163(j)–9(h), this section provides the exclusive rules for allocating tax items that are properly allocable to a trade or business between excepted trades or businesses and non-excepted trades or businesses for purposes of section 163(j). The amount of a taxpayer's interest expense that is properly allocable to excepted trades or businesses is not subject to the section 163(j) limitation. The amount of a taxpayer's other items of income, gain, deduction, or loss, including interest income, that is properly allocable to excepted trades or businesses is excluded from the calculation of the taxpayer's section 163(j) limitation. See section 163(j)(6) and (j)(8)(A)(i); see also § 1.163(j)–1(b)(1)(i)(H), (b)(1)(ii)(F), and (b)(3). The general method of allocation set forth in paragraph (c) of this section is based on the approach that money is fungible and that interest expense is attributable to all activities and property, regardless of any specific purpose for incurring an obligation on which interest is paid. In no event may the amount of interest expense allocated under this section exceed the amount of interest paid or accrued, or treated as paid or accrued, by the taxpayer within the taxable year.

(ii) *Application of section.* The amount of a taxpayer's tax items properly allocable to a trade or business, other than interest expense and interest income, that is properly allocable to excepted trades or businesses for purposes of section 163(j) is determined as set forth in paragraph (b) of this section. The amount of a taxpayer's interest expense and interest income that is properly allocable to excepted trades or businesses for purposes of section 163(j) generally is determined as set forth in paragraph (c) of this section, except as otherwise provided in paragraph (d) of this section. For purposes of this section, a taxpayer's activities are not treated as a separate trade or business to the extent those activities involve the provision of real property, goods, or services to a trade or business of the taxpayer (or, if the taxpayer is a member of a consolidated group, the consolidated group). For example, if a taxpayer engaged in a manufacturing trade or business has in-house legal personnel that provide legal services solely with respect to the taxpayer's manufacturing business, the taxpayer is not treated as also engaged in the trade or business of providing legal services. Similarly, if the taxpayer described in the previous sentence constructs or acquires real property solely for use by the taxpayer's manufacturing business, the taxpayer is not treated as also engaged in a real property trade or business.

(2) *Coordination with other rules*—(i) *In general.* The rules of this section apply after a taxpayer has determined whether any interest expense or interest income paid, received, or accrued is properly allocable to a trade or business. Similarly, the rules of this section apply to other tax items after a taxpayer has determined whether those items are properly allocable to a trade or business. For instance, a taxpayer must apply § 1.163–8T, if applicable, to determine which items of interest expense are investment interest under section 163(d) before applying the rules in paragraph (c) of this section to allocate interest expense between excepted and non-excepted trades or businesses. After determining whether its tax items are properly allocable to a trade or business, a taxpayer that is engaged in both excepted and non-excepted trades or businesses must apply the rules of this section to determine the amount of interest expense that is business interest expense subject to the section 163(j) limitation and to determine which items are included or excluded in computing its section 163(j) limitation.

(ii) *Treatment of investment interest, investment income, investment expenses, and certain other tax items of a partnership with a C corporation or tax-exempt corporation as a partner.* For rules governing the treatment of investment interest, investment income, investment expenses, and certain other separately stated tax items of a partnership with a C corporation or tax-exempt corporation as a partner, see §§ 1.163(j)–4(b)(3) and 1.163(j)–6(k).

(3) *Application of allocation rules to foreign corporations and foreign partnerships.* The rules of this section apply to foreign corporations and foreign partnerships.

(4) *Application of allocation rules to members of a consolidated group*—(i) *In general.* As provided in § 1.163(j)–4(d), the computations required by section 163(j) and the regulations in this part under section 163(j) of the Code generally are made for a consolidated group on a consolidated basis. In this regard, for purposes of applying the allocation rules of this section, all members of a consolidated group are treated as one corporation. Therefore, the rules of this section apply to the activities conducted by the group as if those activities were conducted by a single corporation. For example, the group (rather than a particular member) is treated as engaged in excepted or non-excepted trades or businesses. In the case of intercompany obligations, within the meaning of § 1.1502–13(g)(2)(ii), for purposes of allocating asset basis between excepted and non-excepted trades or businesses, the obligation of the member borrower is not considered an asset of the creditor member. Similarly, intercompany transactions, within the meaning of § 1.1502–13(b)(1)(i), are disregarded for purposes of this section, as are the resulting offsetting items, and property is allocated to a trade or business based on the activities of the group as if the members of the group were divisions of a single corporation. Further, stock of a group member that is owned by another member of the same group is not treated as an asset for purposes of this section, and the transfer of any amount of member stock to a non-member is treated by the group as a transfer of the member's assets proportionate to the amount of member stock transferred. Additionally, stock of a corporation that is not a group member is treated as owned by the group.

(ii) *Application of excepted business percentage to members of a consolidated group.* After a consolidated group has determined the percentage of the group's interest expense allocable to excepted trades or businesses for the taxable year (and thus not subject to the section 163(j) limitation), this exempt percentage is applied to the interest paid or accrued by each member during the taxable year to any lender that is not a group member. Therefore, except to the extent paragraph (d) of this section (providing rules for certain qualified nonrecourse indebtedness) applies, an identical percentage of the interest paid or accrued by each member of the group to any lender that is not a group member is treated as allocable to excepted trades or businesses, regardless of whether any particular member actually engaged in an excepted trade or business.

(iii) *Basis in assets transferred in an intercompany transaction.* For purposes of allocating interest expense and interest income under paragraph (c) of this section, the basis of property does not include any gain or loss realized with respect to the property by another member in an intercompany transaction, as defined in § 1.1502–13(b), whether or not the gain or loss is deferred.

(5) *Tax-exempt organizations.* For tax-exempt organizations, section 512 and the regulations in this part under section 512 of the Code determine the rules for allocating all income and expenses among multiple trades or businesses.

(6) *Application of allocation rules to disallowed disqualified interest.* A taxpayer may apply the allocation rules of this section to disallowed disqualified interest by either:

(i) Applying the allocation rules of this section to all of the taxpayer's disallowed disqualified interest in the taxable year(s) in which the disallowed disqualified interest was paid or accrued (the historical approach); or

(ii) Treating all of the taxpayer's disallowed disqualified interest as if it were paid or accrued in the taxpayer's first taxable year beginning after December 31, 2017 (the effective date approach).

(7) *Examples.* The following examples illustrate the principles of this paragraph (a).

(i) *Example 1: Items properly allocable to a trade or business*—(A) *Facts.* Individual T operates Business X, a non-excepted trade or business, as a sole proprietor. In Year 1, T pays or accrues $40x of interest expense and receives $100x of gross income with respect to Business X that is not eligible for a section 199A deduction. T borrows money to buy a car for personal use, and T pays or accrues $20x of interest expense with respect to the car loan. T also invests in corporate bonds, and, in Year 1, T receives $50x of interest income on those bonds.

(B) *Analysis.* Under paragraphs (a)(1) and (2) of this section, T must determine which items of income and expense, including items of interest income and interest expense, are properly allocable to a trade or business. T's $100x of gross income and T's $40x of interest expense with respect to Business X are properly allocable to a trade or business. However, the interest expense on T's car loan is personal interest within the meaning of section 163(h)(2) rather than interest properly allocable to a trade or business. Similarly, T's interest income from corporate bonds is not properly allocable to a trade or business because it is interest from investment activity. See section 163(d)(4)(B).

(ii) *Example 2: Intercompany transaction*—(A) *Facts.* S is a member of a consolidated group of which P is the common parent. P conducts an electing real property trade or business (Business X), and S conducts a non-excepted trade or business (Business Y). P leases Building V (which P owns) to S for use in Business Y.

(B) *Analysis.* Under paragraph (a)(4)(i) of this section, a consolidated group is treated as a single corporation for purposes of applying the allocation rules of this section, and the consolidated group (rather than a particular member of the group) is treated as engaged in excepted and non-excepted trades or businesses. Thus, intercompany transactions are disregarded for purposes of this section. As a result, the lease of Building V by P to S is disregarded. Moreover, because Building V is used in Business Y, basis in this asset is allocated to Business Y rather than Business X for purposes of these allocation rules, regardless of which member (P or S) owns the building.

(iii) *Example 3: Intercompany sale of natural gas*—(A) *Facts.* S is a member of a consolidated group of which P is the common parent. S drills for natural gas and is not an excepted regulated utility trade or business. S sells most of its natural gas production to P, which produces electricity at its natural gas-fired power plants, and S sells the rest of its natural gas production to third parties at market rates. P is an excepted regulated utility trade or business to the extent that it is engaged in a trade or business described in § 1.163(j)–1(b)(15)(i).

(B) *Analysis.* Intercompany transactions are disregarded for purposes of this section. As a result, the intercompany sales of natural gas by S to P are disregarded. Moreover, the assets of S and P are allocated between the excepted and non-excepted trades or businesses of the P group based on the assets used in each trade or business. Assets of S may be allocated to the P group's excepted trade or business to the extent those assets are used in the trade or business of the furnishing or sale of electrical energy. Likewise, assets of P may be allocated to the P group's non-excepted trade or business to the extent those assets are used in the trade or business of natural gas production.

(iv) *Example 4: Disallowed disqualified interest*—(A) *Facts.* S is a member of a consolidated group of which P is the common parent. P and S are the only members of an affiliated group under old section 163(j)(6)(C). S operates a farm equipment leasing business (Business X) that is not an excepted trade or business. P is engaged in an electing farming business (Business Y). Entering its first taxable year beginning after December 31, 2017, the P group has disallowed disqualified interest of $120x, all of which the P group paid or accrued in earlier taxable years in which it only operated Business X. The P group also incurs $100x of interest expense during its 2018 taxable year, of which $25x (25 percent of $100x) is business interest expense properly allocable to Business X and $75x (75 percent of $100x) is properly allocable to Business Y under paragraph (c) of this section.

(B) *Analysis.* Under paragraph (a)(6) of this section, the P group may allocate disallowed disqualified interest to Business X and Business Y by either applying the allocation rules of this section in the taxable years in which the disallowed disqualified interest was paid or accrued (the historical approach) or by treating such interest as though it were paid or accrued in the P group's first taxable year beginning after December 31, 2017 (the effective date approach). Accordingly, if the P group chooses to rely on the historical approach, it allocates all $120x of disallowed disqualified interest to Business X (a non-excepted trade or business), and all $120x of disallowed disqualified interest is subject to the section 163(j) limitation. If, instead, the P group chooses to rely on the effective date approach, it allocates its $120x of disallowed disqualified interest in the same proportion as its $100x of business interest expense that was paid or accrued in its 2018 taxable year. Of the $120x of disallowed disqualified interest, $30x (25 percent of $120x) is allocated to Business X and $90x (75 percent of $120x) is allocated to Business Y. The $90x of disallowed disqualified interest that is properly allocable to Business Y (an excepted trade or business) is not subject to the section 163(j) limitation.

(b) *Allocation of tax items other than interest expense and interest income*—(1) *In general.* Except as otherwise provided in § 1.163(j)–6(m) or § 1.163(j)–9(h), for purposes of calculating ATI, tax items other than interest expense and interest income are allocated to a particular trade or business in the manner described in this paragraph (b). It is not necessary to allocate items under this paragraph (b) for purposes of calculating ATI if all of the taxpayer's items subject to allocation under this paragraph (b) are allocable to excepted trades or businesses, or if all of those items are allocable to non-excepted trades or businesses.

(2) *Gross income other than dividends and interest income.* A taxpayer's gross income other than dividends and interest income is allocated to the trade or business that generated the gross income.

(3) *Dividends*—(i) *Look-through rule.* If a taxpayer receives a dividend, within the meaning of section 316, that is not investment income, within the meaning of section 163(d), and if the taxpayer satisfies the minimum ownership threshold in paragraph (c)(7) of this section, then, solely for purposes of allocating amounts received as a dividend during the taxable year to excepted or non-excepted trades or

businesses under this paragraph (b), the dividend income is treated as allocable to excepted or non-excepted trades or businesses based upon the relative amounts of the payor corporation's adjusted basis in the assets used in its trades or businesses, determined pursuant to paragraph (c) of this section. If at least 90 percent of the payor corporation's adjusted basis in its assets during the taxable year, determined pursuant to paragraph (c) of this section, is allocable to either excepted trades or businesses or to non-excepted trades or businesses, all of the taxpayer's dividend income from the payor corporation for the taxable year is treated as allocable to either excepted or non-excepted trades or businesses, respectively.

(ii) *Inapplicability of the look-through rule.* If a taxpayer receives a dividend that is not investment income, within the meaning of section 163(d), and if the taxpayer does not satisfy the minimum ownership threshold in paragraph (c)(7) of this section, then the taxpayer must treat the dividend as allocable to a non-excepted trade or business.

(4) *Gain or loss from the disposition of non-consolidated C corporation stock, partnership interests, or S corporation stock*—(i) *Non-consolidated C corporations.* (A) If a taxpayer recognizes gain or loss upon the disposition of stock in a non-consolidated C corporation that is not property held for investment, within the meaning of section 163(d)(5), and if the taxpayer looks through to the assets of the C corporation under paragraph (c)(5)(ii) of this section for the taxable year, then the taxpayer must allocate gain or loss from the disposition of stock to excepted or non-excepted trades or businesses based upon the relative amounts of the C corporation's adjusted basis in the assets used in its trades or businesses, determined pursuant to paragraph (c) of this section. If at least 90 percent of the C corporation's adjusted basis in its assets during the taxable year, determined pursuant to paragraph (c) of this section, is allocable to either excepted trades or businesses or to non-excepted trades or businesses, all of the taxpayer's gain or loss from the disposition is treated as allocable to either excepted or non-excepted trades or businesses, respectively.

(B) If a taxpayer recognizes gain or loss upon the disposition of stock in a non-consolidated C corporation that is not property held for investment, within the meaning of section 163(d)(5), and if the taxpayer does not look through to the assets of the C corporation under paragraph (c)(5)(ii) of this section for the taxable year, then the taxpayer must treat the gain or loss from the disposition of stock as allocable to a non-excepted trade or business.

(C) For rules governing the transfer of stock of a member of a consolidated group, see paragraph (a)(4)(i) of this section.

(ii) *Partnerships and S corporations.* (A) If a taxpayer recognizes gain or loss upon the disposition of interests in a partnership or stock in an S corporation that owns—

(*1*) Non-excepted assets and excepted assets;

(*2*) Investment assets; or

(*3*) Both;

(B) The taxpayer determines a proportionate share of the amount properly allocable to a non-excepted trade or business in accordance with the allocation rules set forth in paragraph (c)(5)(ii)(A) or (c)(5)(ii)(B)(*3*) of this section, as appropriate, and includes such proportionate share of gain or loss in the taxpayer's ATI. However, if at least 90 percent of the partnership's or S corporation's adjusted basis in its assets during the taxable year, determined pursuant to paragraph (c) of this section, is allocable to either excepted trades or businesses or to non-excepted trades or businesses, all of the taxpayer's gain or loss from the disposition is treated as allocable to either excepted or non-excepted trades or businesses, respectively. This rule also applies to tiered passthrough entities by looking through each passthrough entity tier (for example, an S corporation that is the partner of the highest-tier partnership would look through each lower-tier partnership), subject to paragraph (c)(5)(ii)(D) of this section. With respect to a partner that is a C corporation or tax-exempt corporation, a partnership's investment assets are taken into account and treated as non-excepted trade or business assets. For purposes of this paragraph, a passthrough entity means a partnership, S corporation, or any other entity (domestic or foreign) that is not a corporation if all items of income and deduction of the entity are included in the income of its owners or beneficiaries.

(5) *Expenses, losses, and other deductions*—(i) *Expenses, losses, and other deductions that are definitely related to a trade or business.* Expenses (other than interest expense), losses, and other deductions (collectively, *deductions* for purposes of this paragraph (b)(5)) that are definitely related to a trade or business are allocable to the trade or business to which they relate. A deduction is considered definitely related to a trade or business if the item giving rise to the deduction is incurred as a result of, or incident to, an activity of the trade or business or in connection with property used in the trade or business (see § 1.861–8(b)(2)). If a deduction is definitely related to one or more excepted trades or businesses and one or more non-excepted trades or businesses, the deduction is apportioned between the excepted and non-excepted trades or businesses based upon the relative amounts of the taxpayer's adjusted basis in the assets used in those trades or businesses, as determined under paragraph (c) of this section.

(ii) *Other deductions.* Deductions that are not described in paragraph (b)(5)(i) of this section are ratably apportioned based on the gross income of each trade or business.

(6) *Treatment of investment items and certain other items of a partnership with a C corporation partner.* Any investment income, investment expense, or other item that a partnership receives, pays, or accrues and that is treated as properly allocable to a trade or business of a C corporation partner under § 1.163(j)–4(b)(3)(i) is treated as properly allocable to a non-excepted trade or business of the C corporation partner, except that any item with respect to property or activities for which an election has been made by the partnership under § 1.163(j)–9(b) is treated as properly allocable to an excepted trade or business. See, for example, an election for activities described in § 1.163(j)–9(b)(2)(ii) or an election under § 1.163(j)–9(h).

(7) *Examples: Allocation of income and expense.* The following examples illustrate the principles of this paragraph (b):

(i) *Example 1: Allocation of income and expense between excepted and non-excepted trades or businesses*—(A) *Facts.* T conducts an electing real property trade or business (Business Y), which is an excepted trade or business. T also operates a lumber yard (Business Z), which is a non-excepted trade or business. In Year 1, T receives $100x of gross rental income from real property leasing activities. T also pays or accrues $60x of expenses in connection with its real property leasing activities and $20x of legal services performed on behalf of both Business Y and Business Z. T receives $60x of gross income from lumber yard customers and pays or accrues $50x of expenses related to the lumber yard business. For purposes of expense allocations under paragraphs (b) and (c) of this section, T has $240x of adjusted basis in its Business Y assets and $80x of adjusted basis in its Business Z assets.

(B) *Analysis.* Under paragraph (b)(2) of this section, for Year 1, $100x of rental income is allocated to Business Y, and $60x of income from lumber yard customers is allocated to Business Z. Under paragraph (b)(5)(i) of this section, $60x of expenses paid or accrued in connection with real property leasing activities are allocated to Business Y, and $50x of expenses related to the lumber yard are allocated to Business Z. The $20x of remaining expenses for legal services performed on behalf of both Business Y and Business Z are allocated according to the relative amounts of T's basis in the assets used in each business. The total amount of T's basis in the assets used in Businesses Y and Z is $320x, of which 75 percent ($240x/$320x) is used in Business Y and 25 percent ($80x/$320x) is used in Business Z. Accordingly, $15x of the expenses for legal services are allocated to Business Y and $5x are allocated to Business Z.

(ii) *Example 2: Allocation of partnership items from investment activity*—(A) *Facts.* U, a domestic C corporation, directly conducts an electing real property trade or business. U also has an interest in PRS, a partnership that holds real property for investment. PRS's investment in real property is not a trade or business under section 162 or a real property trade or business under section 469. During the taxable year, PRS sells some of its real property to third parties and allocates $80x of income to U from these sales. In addition, PRS incurs deductible expenses related to its investment in real property and allocates $9x of these deductible expenses to U.

(B) *Analysis.* Under paragraph (b)(6) of this section, any investment income or investment expense that a partnership receives, pays, or accrues and that is treated as properly allocable to a trade or business of a C corporation partner is treated as properly allocable to a non-excepted trade or business of the C corporation partner. Because PRS generates its income and expense from investment activity that is not a trade or business under section 162 or a real property trade or business under section 469, U's allocation of $80x of income and $9x of deductible expense from PRS is treated as properly allocable to a non-excepted trade or business.

(c) *Allocating interest expense and interest income that is properly allocable to a trade or business*—(1) *General rule*—(i) *In general.* Except as otherwise provided in this section, § 1.163(j)–6(m), or § 1.163(j)–9(h), the amount of a taxpayer's interest expense and interest income that is properly allocable to a trade or business is allocated to the taxpayer's excepted or non-excepted trades or businesses for purposes of section 163(j) based upon the relative amounts of the taxpayer's adjusted basis in the assets, as determined under paragraph (c)(5) of this section, used in its excepted or non-excepted trades or businesses. The taxpayer must determine the adjusted basis in its assets as of the close of each determination date, as defined in paragraph (c)(6) of this section, in the taxable year and average those amounts to determine the relative amounts of asset basis for its excepted and non-excepted trades or businesses for that year. It is not necessary to allocate interest expense or interest income under this paragraph (c) for purposes of determining a taxpayer's business interest expense and business interest income if all of the taxpayer's interest income and expense is allocable to excepted trades or businesses (in which case the taxpayer is not subject to the section 163(j) limitation) or if all of the taxpayer's interest income and expense is allocable to non-excepted trades or businesses.

(ii) *De minimis exception.* If at least 90 percent of the taxpayer's basis in its assets for the taxable year is allocable to either excepted or non-excepted trades or businesses pursuant to this paragraph (c), then all of the taxpayer's interest expense and interest income for that year that is properly allocable to a trade or business is treated as allocable to either excepted or non-excepted trades or businesses, respectively.

(2) *Example.* The following example illustrates the principles of paragraph (c)(1) of this section:

(i) *Facts.* T is a calendar-year C corporation engaged in an electing real property trade or business, the business of selling wine, and the business of selling hand-carved wooden furniture. In Year 1, T has $100x of interest expense that is deductible except for the potential application of section 163(j). Based upon determinations made on the determination dates in Year 1, T's average adjusted basis in the assets used in the electing real property trade or business (an excepted trade or business) in Year 1 is $800x, and T's total average adjusted basis in the assets used in the other two businesses (which are non-excepted trades or businesses) in Year 1 is $200x.

(ii) *Analysis.* $80x (($800x/($800x + $200x)) × $100x) of T's interest expense for Year 1 is allocable to T's electing real property trade or business and is not business interest expense subject to the section 163(j) limitation. The remaining $20x of T's interest expense is business interest expense for Year 1 that is subject to the section 163(j) limitation.

(3) *Asset used in more than one trade or business*—(i) *General rule.* If an asset is used in more than one trade or business during a determination period, as defined in paragraph (c)(6) of this section, the taxpayer's adjusted basis in the asset is allocated to each trade or business using the permissible methodology under this paragraph (c)(3) that most reasonably reflects the use of the asset in each trade or business during that determination period. An allocation methodology most reasonably reflects the use of the asset in each trade or business if it most properly reflects the proportionate benefit derived from the use of the asset in each trade or business. A taxpayer is not required to use the same allocation methodology for each type of asset used in a trade a business. Instead, a taxpayer may use different allocation methodologies for different types of assets used in a trade or business. If none of the permissible methodologies set forth in paragraph (c)(3)(ii) of this section reasonably reflects the use of the asset in each trade or business, the taxpayer's basis in the asset is not taken into account for purposes of this paragraph (c).

(ii) *Permissible methodologies for allocating asset basis between or among two or more trades or businesses.* Subject to the special rules in paragraphs (c)(3)(iii) and (c)(5) of this section, a taxpayer's basis in an asset used in two or more trades or businesses during a determination period may be allocated to those trades or businesses based upon—

(A) The relative amounts of gross income that an asset generates, has generated, or may reasonably be expected to generate, within the meaning of § 1.861–9T(g)(3), with respect to the trades or businesses;

(B) If the asset is land or an inherently permanent structure, the relative amounts of physical space used by the trades or businesses; or

(C) If the trades or businesses generate the same unit of output, the relative amounts of output of those trades or businesses (for example, if an asset is used in two trades or businesses, one of which is an excepted regulated utility trade or business, and the other of which is a non-excepted regulated utility trade or business, the taxpayer may allocate basis in the asset based upon the relative amounts of kilowatt-hours generated by each trade or business).

(iii) *Special rules*—(A) *Consistent allocation methodologies*—(*1*) *In general.* Except as otherwise provided in paragraph (c)(3)(iii)(A)(*2*) of this section, a taxpayer must maintain the same allocation methodology for a period of at least five taxable years.

(*2*) *Consent to change allocation methodology.* If a taxpayer has used the same allocation methodology for at least five taxable years, the taxpayers may change its method of allocation under paragraphs (c)(3)(i) and (ii) of this section without the consent of the Commissioner. If a taxpayer has used the same allocation methodology for less than five taxable years, and if the taxpayer determines that a different allocation methodology properly reflects the proportionate benefit derived from the use of assets in its trades or businesses, the taxpayer may change its method of allocation under paragraphs (c)(3)(i) and (ii) of this section only with the consent of the Commissioner. To obtain consent, a taxpayer must submit a request for a letter ruling under the applicable administrative procedures, and consent will be granted only in extraordinary circumstances.

(B) *De minimis exception.* If at least 90 percent of the taxpayer's basis in an asset would be allocated to either excepted trades or businesses or non-excepted trades or businesses during a determination period pursuant to this paragraph (c)(3), the taxpayer's entire basis in the asset for the determination period must be allocated to either excepted or non-excepted trades or businesses, respectively. This rule applies before the application of paragraph (c)(1)(ii) of this section.

(C) *Allocations of excepted regulated utility trades or businesses*—(*1*) *In general.* Except as provided in the de minimis rule in paragraph (c)(3)(iii)(C)(*3*) of this section, a taxpayer is engaged in an excepted regulated utility trade or business only to the extent that the taxpayer is engaged in an excepted regulated utility trade or business described in § 1.163(j)–1(b)(15)(i)(A), (B), or (C), and any remaining utility trade or business is a non-excepted trade or business. Thus, for example, electricity sold by a utility trade or business at rates not established or approved by an entity described in § 1.163(j)–1(b)(15)(i)(A)(*2*) and not subject to an election under § 1.163(j)–1(b)(15)(iii) must be treated as electricity sold by a non-excepted regulated utility trade or business. The taxpayer must allocate under this paragraph (c) the basis of assets used in the utility trade or business between its excepted and non-excepted trades or businesses.

(*2*) *Permissible method for allocating asset basis for utility trades or businesses.* In the case of a utility trade or business described in paragraph (c)(3)(iii)(C)(*1*) of this section, and except as provided in the de minimis rule in paragraph (c)(3)(iii)(C)(*3*) of this section, the method described in paragraph (c)(3)(ii)(C) of this section is the only permissible method under this paragraph (c)(3) for allocating the taxpayer's basis in assets used in both the excepted and non-excepted trades or businesses of selling or furnishing the items described in § 1.163(j)–1(b)(15)(i)(A)(*1*).

(*3*) *De minimis rule for excepted utility trades or businesses.* If a taxpayer is engaged in a utility trade or business described in paragraph (c)(3)(iii)(C)(*1*) of this section, and if at least 90 percent of the items described in § 1.163(j)–1(b)(15)(i)(A)(*1*) are furnished or sold by trades or businesses described in § 1.163(j)–1(b)(15)(i)(A), (B) or (C), the taxpayer's entire trade or business is an excepted regulated utility trade or business, and paragraph (c)(3)(iii)(C)(*2*) of this section does not apply. This rule applies before the application of paragraph (c)(3)(iii)(B) of this section.

(*4*) *Example.* The following example illustrates the principles of this paragraph (c)(3)(iii)(C):

(*i*) *Facts.* X, a C corporation, is engaged in the trade or business of generating electrical energy. During each determination period in the taxable year, 80 percent of the megawatt-hours generated in the electricity generation trade or business is sold at rates negotiated with the purchaser, and with respect to which X filed a schedule of rates with a public utility commission. The public utility commission has the authority to take action on the filed schedule of rates, but if no action is taken, the rules governing the public utility commission explicitly state that the public utility commission is deemed to have approved the rates. The public utility has taken no action with respect to the negotiated rate. The remaining 20 percent of the megawatt-hours is sold on the wholesale market at rates not established or subject to approval by a regulator described in § 1.163(j)–1(b)(15)(i)(A)(*2*). X has not made an election under § 1.163(j)–1(b)(15)(iii). None of the assets used in X's utility generation trade or business are used in any other trade or business.

(*ii*) *Analysis.* For purposes of section 163(j), under paragraph (c)(3)(iii)(C)(*1*) of this section, 80 percent of X's electricity generation business is an excepted regulated utility trade or business, because the rate for the sale of the electricity was subject to approval by a regulator described in § 1.163(j)–1(b)(15)(i)(A)(*2*). The remaining 20 percent of X's business is a non-excepted utility trade or business. Under paragraph (c)(3)(iii)(C)(*2*) of this section, X must allocate 80 percent of the basis of the assets used in its utility business to excepted trades or business and the remaining 20 percent of the basis in the assets to non-excepted trades or businesses.

(D) *Special allocation rule for real property trades or businesses subject to special anti-abuse rule*—(*1*) *In general.* In the case of a trade or business that leases real property subject to an arrangement described in § 1.163(j)–9(j)(1), including trades or businesses to which the look-through exception in § 1.163(j)–9(j)(2)(ii) applies, the taxpayer must allocate under this paragraph (c)(3) the basis of property used in both the excepted and non-excepted portions of its trade or business, as determined under § 1.163(j)–9(j)(3).

(*2*) *Allocation methodology for real property.* For purposes of this paragraph (c)(3)(iii)(D), a taxpayer must allocate the basis of real property leased under an arrangement described in § 1.163(j)–9(j)(1) or (j)(2)(i) between the excepted and non-excepted portions of the real property trade or business based on the relative fair market rental value of the real property that is attributable to the excepted and non-excepted portions of the trade or business, respectively.

(*3*) *Example.* The following example illustrates the principles of this paragraph (c)(3)(iii)(D):

(*i*) *Facts.* X and Y are domestic C corporations under common control within the meaning of section 267(b), but neither X nor Y are members of a consolidated group. The small business exemption in § 1.163(j)–2(d) does not apply to X or Y. X owns an office building and leases the entire building to Y. Y subleases 80 percent of the office building, measured by fair market rental value, to a related party. Y subleases the remaining 20 percent of the building to unrelated third parties. X also owns depreciable scaffolding equipment, which it uses to clean all of the building's windows as part of its leasing arrangement with Y.

(*ii*) *Analysis.* Under § 1.163(j)–9(j)(2)(ii), X is eligible to make an election for 20 percent of its business of leasing the office building to be an electing real property trade or business. Assuming X makes such an election, X must allocate the basis of assets used in both the excepted and non-excepted portions of its leasing trade or business under this paragraph (c). Under paragraph (c)(3)(iii)(D)(*2*) of this section, X must allocate the basis of the office building based on the relative fair market value attributable to the excepted and non-excepted portions of its leasing business. Therefore, X must allocate 20 percent of the basis of the building to the excepted portion of its leasing business, and it must allocate the remaining 80 percent of the building to the non-excepted portion of its leasing business. Under paragraph (c)(3)(iii)(D)(*2*) of this section, X may use one of the allocation methods described in paragraph (c)(3)(ii) of this section to allocate the basis of its scaffolding equipment between the excepted and non-excepted portions of its leasing trade or business.

(4) *Disallowed business interest expense carryforwards; floor plan financing interest expense.* Disallowed business interest expense carryforwards (which were treated as allocable to a non-excepted trade or business in a prior taxable year) are not re-allocated between non-excepted and excepted trades or businesses in a succeeding taxable year. Instead, the carryforwards continue to be treated as allocable to a non-excepted trade or business. Floor plan financing interest expense also is not subject to allocation between excepted and non-excepted trades or businesses (see § 1.163(j)–1(b)(19)) and is always treated as allocable to non-excepted trades or businesses.

(5) *Additional rules relating to basis*—(i) *Calculation of adjusted basis*—(A) *Non-depreciable property other than land.* Except as otherwise provided in paragraph (c)(5)(i)(E) of this section, for purposes of this section, the adjusted basis of an asset other than land with respect to which no deduction is allowable under section 167, former section 168, or section 197, as applicable, is the adjusted basis of the asset for determining gain or loss from the sale or other disposition of that asset as provided in § 1.1011–1. Self-created intangible assets are not taken into account for purposes of this paragraph (c).

(B) *Depreciable property other than inherently permanent structures.* For purposes of this section, the adjusted basis of any tangible asset with respect to which a deduction is allowable under section 167, other than inherently permanent structures, is determined by using the alternative depreciation system under section 168(g) before any application of the additional first-year depreciation deduction (for example, under section 168(k) or (m)), and the adjusted basis of any tangible asset with respect to which a deduction is allowable under former section 168, other than inherently permanent structures, is determined by using the taxpayer's method of computing depreciation for the asset under former section 168. The depreciation deduction with respect to the property described in this paragraph (c)(5)(i)(B) is allocated ratably to each day during the period in the taxable year to which the depreciation relates. A change to the alternative depreciation system should be determined in a manner similar to that in § 1.168(i)–4(d)(4) or (d)(5)(ii)(B), as applicable.

(C) *Special rule for land and inherently permanent structures.* Except as otherwise provided in paragraph (c)(5)(i)(E) of this section, for purposes of this section, the adjusted basis of any asset that is land, including nondepreciable improvements to land, or an inherently permanent structure is its unadjusted basis.

(D) *Depreciable or amortizable intangible property and depreciable income forecast method property.* For purposes of this section, the adjusted basis of any intangible asset with respect to which a deduction is allowable under section 167 or 197, as applicable, is determined in accordance with section 167 or 197, as applicable, and the adjusted basis of any asset described in section 167(g)(6) for which a deduction is allowable under section 167 is determined in accordance with section 167(g). The adjusted basis of any intangible asset under this paragraph (c)(5)(i)(D) is determined before any application of the additional first-year depreciation deduction. The depreciation or amortization deduction with respect to the property described in this paragraph (c)(5)(i)(D) is allocated ratably to each day during the period in the taxable year to which the depreciation or amortization relates.

(E) *Assets not yet used in a trade or business.* Assets that have been acquired or that are under development but that are not yet used in a trade or business are not taken into account for purposes of this paragraph (c). For example, construction works in progress (such as buildings, airplanes, or ships) are not taken into account for purposes of this paragraph (c). Similarly, land acquired by a taxpayer for construction of a building by the taxpayer to be used in a trade or business is not taken into account for purposes of under this paragraph (c) until the building is placed in service. This rule does not apply to interests in a partnership or stock in a corporation.

(F) *Trusts established to fund specific liabilities.* Trusts required to fund specific liabilities (for example, pension trusts, and nuclear decommissioning funds (including, but not limited to, those funds for which an election is made under section 468A)) are not taken into account for purposes of this paragraph (c).

(G) *Inherently permanent structure.* For purposes of this section, the term *inherently permanent structure* has the meaning provided in § 1.856–10(d)(2).

(ii) *Partnership interests; stock in non-consolidated C corporations*—(A) *Partnership interests*—(*1*) *Calculation of asset basis.* For purposes of this section, a partner's interest in a partnership is treated as an asset of the partner. For these purposes, the partner's adjusted basis in a partnership interest is reduced, but not below zero, by the partner's share of partnership liabilities, as determined under section 752, and is further reduced as provided in paragraph (c)(5)(ii)(A)(*2*)(*iii*) of this section. If a partner elects or is required to apply the rules in this paragraph (c)(5)(ii)(A) to look through to a partnership's basis in the partnership's assets, the partner's basis in the partnership interest is adjusted to the extent of the partner's share of any adjustments to the basis of the partnership's assets required pursuant to the rules in paragraph (c)(5)(i) of this section.

(*2*) *Allocation of asset basis*—(*i*) *In general.* For purposes of determining the extent to which a partner's adjusted basis in its partnership interest is allocable to an excepted or non-excepted trade or business, the partner may look through to such partner's share of the partnership's basis in the partnership's assets, taking into account any adjustments under sections 734(b) and 743(b), and adjusted to the extent required under paragraph (d)(4) of this section, except as otherwise provided in paragraph (c)(5)(ii)(D) of this section. For purposes of the preceding sentence, such partner's share of partnership assets is determined using a reasonable method taking into account special allocations under section 704(b). Notwithstanding paragraph (c)(7) of this section, if a partner's direct and indirect interest in a partnership is greater than or equal to 80 percent of the partnership's capital or profits, the partner must apply the rules in this paragraph (c)(5)(ii)(A)(*2*) to look through to the partnership's basis in the partnership's assets. If a partner elects or is required to apply the rules in this paragraph (c)(5)(ii)(A)(*2*) to look through to a partnership's basis in the partnership's assets, the partner allocates the basis of its partnership interest between excepted and non-excepted trades or businesses based on the ratio in which the partner's share of the partnership's adjusted tax basis in its trade or business assets is allocated between excepted and non-excepted trade or business assets.

(*ii*) *De minimis rule.* If, after applying paragraph (c)(5)(ii)(A)(*2*)(*iii*) of this section, at least 90 percent of a partner's share of a partnership's basis in its assets (including adjustments under sections 734(b) and 743(b)) is allocable to either excepted trades or businesses or non-excepted trades or businesses, without regard to assets not properly allocable to a trade or business, the partner's entire basis in its partnership interest is treated as allocable to either excepted or non-excepted trades or businesses, respectively. For purposes of the preceding sentence, such partner's share of partnership assets is determined using a reasonable method taking into account special allocations under section 704(b).

(*iii*) *Partnership assets not properly allocable to a trade or business.* For purposes of applying paragraphs (c)(5)(ii)(A)(*2*)(*i*) and (*ii*) of this section to a partner that is a C corporation or tax-exempt corporation, such partner's share of a partnership's assets that are not properly allocable to a trade or business is treated as properly allocable to a non-excepted trade or business of such partner. However, if the partnership made an election under § 1.163(j)–9(b) or § 1.163(j)–9(h) with respect to an asset or activity, the assets (or assets related to such activities) are treated as properly allocable to an excepted trade or business of such partner. See, for example, an election under § 1.163(j)–9(h) for an asset or an election under § 1.163(j)–9(b) with respect to activities described in § 1.163(j)–9(b)(2)(ii). For a partner other than a C corporation or tax-exempt corporation, a partnership's assets that are not properly allocable to a trade or business are treated as neither excepted nor non-excepted trade or business assets; instead, such partner's adjusted basis in its partnership interest is decreased by that partner's share of the excess of the partnership's basis in those assets over the partnership's debt that is traced to such assets in accordance with § 1.163–8T, and it is increased by that partner's share of the excess of the partnership's debt that is traced to such assets in accordance with § 1.163–8T over the partnership's basis in those assets. For purposes of the preceding sentence, the partnership's asset basis in property not allocable to a trade or business is adjusted pursuant to the rules in paragraph (c)(5)(i) of this section. For purposes of this paragraph (c)(5)(ii)(A)(*2*)(*iii*), such partner's share of a partnership's assets is determined under a reasonable method taking into account special allocations under section 704(b).

(*iv*) *Inapplicability of partnership look-through rule.* If a partner, other than a C corporation or a tax-exempt corporation, chooses not to look through to the partnership's basis in the partnership's assets under paragraph (c)(5)(ii)(A)(*2*)(*i*) of this section or is precluded by paragraph (c)(5)(ii)(D) of this section from applying such partnership look-through rule, the partner generally will treat its basis in the partnership interest as either an asset held for investment or a non-excepted trade or business asset as determined under section 163(d). If a partner that is a C corporation or a tax-exempt corporation chooses not to look through to the partnership's basis in the partnership's assets under paragraph (c)(5)(ii)(A)(*2*)(*i*) of this section or is precluded by paragraph (c)(5)(ii)(D) of this section from applying such partnership look-through rule, the taxpayer must treat its entire basis in the partnership interest as allocable to a non-excepted trade or business.

(B) *Stock in domestic non-consolidated corporations*—(*1*) *In general.* For purposes of this section, if a taxpayer owns stock in a domestic C corporation that is not a member of the taxpayer's consolidated group, or if the taxpayer owns stock in an S corporation, the stock is treated as an asset of the taxpayer.

(*2*) *Domestic non-consolidated C corporations*—(*i*) *Allocation of asset basis.* If a shareholder satisfies the minimum ownership threshold in paragraph (c)(7) of this section for stock in a domestic non-consolidated C corporation, and if dividends paid on such stock would not be included in the shareholder's investment income under section 163(d)(4)(B), then, for purposes of determining the extent to which the shareholder's basis in the stock is allocable to an excepted or non-excepted trade or business, the shareholder must look through to the corporation's basis in the corporation's assets, adjusted to the extent required under paragraph (d)(4) of this section, except as otherwise provided in paragraph (c)(5)(ii)(D) of this section. If a shareholder does not satisfy the minimum ownership threshold in paragraph (c)(7) of this section for stock in a domestic non-consolidated C corporation, but the shareholder's direct and indirect interest in such corporation is greater than or equal to 80 percent by value, and if dividends paid on such stock would not be included in the shareholder's investment income under section 163(d)(4)(B), then, for purposes of determining the extent to which the shareholder's basis in the stock is allocable to an excepted or non-excepted trade or business, the shareholder may look through to the corporation's basis in the corporation's assets, adjusted to the extent required under paragraph (d)(4) of this section, except as otherwise provided in paragraph (c)(5)(ii)(D) of this section. For purposes of the preceding sentence, indirect stock ownership is determined by applying the constructive ownership rules of section 318(a).

(*ii*) *De minimis rule.* If at least 90 percent of the domestic non-consolidated C corporation's basis in the corporation's assets is allocable to either excepted trades or businesses or non-excepted trades or businesses, the shareholder's entire interest in the corporation's stock is treated as allocable to either excepted or non-excepted trades or businesses, respectively.

(*iii*) *Inapplicability of corporate look-through rule.* If a shareholder other than a C corporation or a tax-exempt corporation is ineligible to look through or chooses not to look through to a corporation's basis in its assets under paragraph (c)(5)(ii)(B)(*2*)(*i*) of this section, the shareholder generally will treat its entire basis in the corporation's stock as an asset held for investment. If a shareholder that is a C corporation or a tax-exempt corporation is ineligible to look through or chooses not to look through to a corporation's basis in its assets under paragraph (c)(5)(ii)(B)(*2*)(*i*) of this section, the shareholder must treat its entire basis in the corporation's stock as allocable to a non-excepted trade or business.

(*iv*) *Use of inside basis for purposes of C corporation look-through rule.* This paragraph (c)(5)(ii)(B)(*2*)(*iv*) applies if a shareholder meets the requirements to look through the stock of a domestic non-consolidated C corporation under paragraph (c)(5)(ii)(B)(*2*)(*i*) of this section, determined without applying the constructive ownership rules of section 318(a). If this paragraph (c)(5)(ii)(B)(*2*)(*iv*) applies, then solely for purposes of allocating asset basis under paragraph (c)(5)(ii)(B)(*2*)(*i*) of this section, and except as otherwise provided in paragraph (c)(5)(ii)(D) of this section, the shareholder may look through to such shareholder's pro rata share of the C corporation's basis in its assets, taking into account the modifications in paragraph (c)(5)(i) of this section with respect to the C corporation's assets, and adjusted to the extent required under paragraph (d)(4) of this section (asset basis look-through approach). If a shareholder applies the asset basis look-through approach, it must do so for all domestic non-consolidated C corporations for which the shareholder is eligible to use this approach, and it must report its use of this approach on the information statement described in paragraph (c)(6)(iii) of this section. The shareholder also must continue to use the asset basis look-through approach in all future taxable years in which the shareholder is eligible to use this approach.

(*3*) *S corporations*—(*i*) *Calculation of asset basis.* For purposes of this section, a shareholder's share of stock in an S corporation is treated as an asset of the shareholder. Additionally, for these purposes, the shareholder's adjusted basis in a share of S corporation stock is adjusted to take into account the modifications in paragraph (c)(5)(i) of this section with respect to the assets of the S corporation (for example, a shareholder's adjusted basis in its S corporation stock is increased by the shareholder's share of depreciation with respect to an inherently permanent structure owned by the S corporation).

(*ii*) *Allocation of asset basis.* For purposes of determining the extent to which a shareholder's basis in its stock of an S corporation is allocable to an excepted or non-excepted trade or business, the shareholder may look through to such shareholder's share of the S corporation's basis in the S corporation's assets, allocated on a pro rata basis, adjusted to the extent required under paragraph (d)(4) of this section, except as otherwise provided in paragraph (c)(5)(ii)(D) of this section. Notwithstanding paragraph (c)(7) of this section, if a shareholder's direct and indirect interest in an S corporation is greater than or equal to 80 percent of the S corporation's stock by vote and value, the shareholder must apply the rules in this paragraph (c)(5)(ii)(B)(*3*) to look through to the S corporation's basis in the S corporation's assets. For these purposes, indirect stock ownership is determined by applying the constructive ownership rules of section 318(a).

(*iii*) *De minimis rule.* If at least 90 percent of a shareholder's share of an S corporation's basis in its assets is allocable to either excepted trades or businesses or non-excepted trades or businesses, the shareholder's entire basis in its S corporation stock is treated as allocable to either excepted or non-excepted trades or businesses, respectively.

(*iv*) *Inapplicability of S corporation look-through rule.* If a shareholder chooses not to look through to the S corporation's basis in the S corporation's assets under paragraph (c)(5)(ii)(B)(*3*)(*ii*) of this section or is precluded by paragraph (c)(5)(ii)(D) of this section from applying such S corporation look-through rule, the shareholder will treat its basis in the S corporation stock as either an asset held for investment or a non-excepted trade or business asset as determined under section 163(d).

(C) *Stock in relevant foreign corporations*—(*1*) *In general.* The rules applicable to domestic non-consolidated C corporations in paragraph (c)(5)(ii)(B) of this section also apply to relevant foreign corporations (as defined in § 1.163(j)–1(b)(33)).

(*2*) *Special rule for CFC utilities.* Solely for purposes of applying the rules in paragraph (c)(5)(ii)(B) of this section, a utility trade or business conducted by an applicable CFC is treated as an excepted regulated utility trade or business, but only to the extent that the applicable CFC sells or furnishes the items described in § 1.163(j)–1(b)(15)(i)(A)(*1*) pursuant to rates established or approved by an entity described in § 1.163(j)–1(b)(15)(i)(A)(*2*), a foreign government, a public service or public utility commission or other similar body of any foreign government, or the governing or ratemaking body of a foreign electric cooperative. For purposes of this paragraph (c)(5)(ii)(C)(*2*), the term *foreign government* means any foreign government, any political subdivision of a foreign government, or any wholly owned agency or instrumentality of any one of the foregoing within the meaning of § 1.1471–6(b).

(D) *Inapplicability of look-through rule to partnerships or non-consolidated C corporations to which the small business exemption applies.* A taxpayer may not apply the look-through rules in paragraphs (b)(3) and (c)(5)(ii)(A), (B), and (C) of this section to a partnership, S corporation, or non-consolidated C corporation that is eligible for the small business exemption under section 163(j)(3) and § 1.163(j)–2(d)(1), unless the partnership, S corporation, or non-consolidated C corporation elects under § 1.163(j)–9 for a trade or business to be an electing real property trade or business or an electing farming business.

(E) *Tiered entities.* If a taxpayer applies the look-through rules of this paragraph (c)(5)(ii), the taxpayer must do so for all lower-tier entities with respect to which the taxpayer satisfies, directly or indirectly, the minimum ownership threshold in paragraph (c)(7) of this section, subject to the limitation in paragraph (c)(5)(ii)(D) of this section, beginning with the lowest-tier entity.

(iii) *Cash and cash equivalents and customer receivables.* Except as otherwise provided in the last sentence of this paragraph (c)(5)(iii), a taxpayer's basis in its cash and cash equivalents and customer receivables is not taken into account for purposes of this paragraph (c). This rule also applies to a lower-tier entity if a taxpayer looks through to the assets of that entity under paragraph (c)(5)(ii) of this section. For purposes of this paragraph (c)(5)(iii), the term *cash and cash equivalents* includes cash, foreign currency, commercial paper, any interest in an investment company registered under the Investment Company Act of 1940 (1940 Act) and regulated as a money market fund under 17 CFR 270.2a–7 (Rule 2a–7 under the 1940 Act), any obligation of a government, and any derivative that is substantially secured by an obligation of a government, or any similar asset. For purposes of this paragraph (c)(5)(iii), a *derivative* is a derivative described in section 59A(h)(4)(A), without regard to section 59A(h)(4)(C). For purposes of this paragraph (c)(5)(iii), the term *government* means the United States or any agency or instrumentality of the United States; a State, a territory, a possession of the United States, the District of Columbia, or any political subdivision thereof within the meaning of section 103 and § 1.103–1; or any foreign government, any political subdivision of a foreign government, or any wholly owned agency or instrumentality of any one of the foregoing within the meaning of § 1.1471–6(b). This paragraph (c)(5)(iii) does not apply to an entity that qualifies as a financial services entity as described in § 1.904–4(e)(3).

(iv) *Deemed asset sale.* Solely for purposes of determining the amount of basis allocable to excepted and non-excepted trades or businesses under this section, an election under section 336, 338, or 754, as applicable, is deemed to have been made for any acquisition of corporate stock or partnership interests with respect to which the taxpayer demonstrates, in the information statement required by paragraph (c)(6)(iii)(B) of this section, that the acquisition qualified for such an election and that, immediately before the acquisition, the acquired entity had a regulatory liability for deferred taxes recorded on its books with respect to property predominantly used in an excepted regulated utility trade or business. Any additional basis taken into account under this rule is reduced ratably over a 15-year period beginning with the month of the acquisition and is not subject to the anti-abuse rule in paragraph (c)(8) of this section.

(v) *Other adjustments.* The Commissioner may make appropriate adjustments to prevent a taxpayer from intentionally and artificially increasing its basis in assets attributable to an excepted trade or business.

(6) *Determination dates; determination periods; reporting requirements*—(i) *Determination dates and determination periods*—(A) *Quarterly determination periods.* For purposes of this section, and except as otherwise provided in paragraph (c)(6)(i)(B) of this section, the term *determination date* means the last day of each quarter of the taxpayer's taxable year (and the last day of the taxpayer's taxable year, if the taxpayer has a short taxable year), and the term *determination period* means the period beginning the day after one determination date and ending on the next determination date.

(B) *Annual determination periods.* If a taxpayer satisfies the requirements of the last sentence of this paragraph (c)(6)(i)(B), the taxpayer may allocate asset basis for a taxable year based on the average of adjusted asset basis at the beginning of the year and the end of the year (annual determination method). For these purposes, the term *determination date* means the last day of the taxpayer's taxable year, and the term *determination period* has the same meaning as provided in paragraph (c)(6)(i)(A) of this section. A taxpayer may use the annual determination method for a taxable year only if the taxpayer demonstrates that its total adjusted basis (as determined under paragraph (c)(5) of this section) at the end of the year in its assets used in its excepted trades or businesses, as a percentage of the taxpayer's total adjusted basis at the end of such year in all of its assets used in a trade or business, does not differ by more than 20 percent from such percentage at the beginning of the year.

(ii) *Application of look-through rules.* If a taxpayer that applies the look-through rules of paragraph (c)(5)(ii) of this section has a different taxable year than the partnership or non-consolidated C corporation to which the taxpayer is applying those rules, then, for purposes of this paragraph (c)(6), the taxpayer must use the most recent asset basis figures from the partnership or non-consolidated C corporation. For example, assume that PS1 is a partnership with a May 31 taxable year, and that C (a calendar-year C corporation that is ineligible to use the annual determination method for the taxable year) is a partner in PS1. PS1's determination dates are February 28, May 31, August 31, and November 30. In turn, C's determination dates are March 31, June 30, September 30, and December 31. If C looks through to PS1's basis in its assets under paragraph (c)(5)(ii) of this section, then, for purposes of determining the amount of C's asset basis that is attributable to its excepted and non-excepted businesses on March 31, C must use PS1's asset basis calculations for February 28.

(iii) *Reporting requirements*—(A) *Books and records.* A taxpayer must maintain books of account and other records and data as necessary to substantiate the taxpayer's use of an asset in an excepted trade or business and to substantiate any adjustments to asset basis for purposes of applying this paragraph (c). One indication that a particular asset is used in a particular trade or business is if the taxpayer maintains separate books and records for all of its excepted and non-excepted trades or businesses and can show the asset in the books and records of a particular excepted or non-excepted trade or business. For rules governing record retention, see § 1.6001–1.

(B) *Information statement.* Except as otherwise provided in publications, forms, instructions, or other guidance, each taxpayer that is making an allocation under this paragraph (c), including any taxpayer that satisfies the de minimis rule in paragraph (c)(1)(ii) of this section, must prepare a statement titled ''Section 163(j) Asset Basis Calculations'' containing the information described in paragraphs (c)(6)(iii)(B)(*1*) through (*7*) of this section and must attach the statement to its timely filed Federal income tax return for the taxable year:

(*1*) The taxpayer's adjusted basis in the assets used in its excepted and non-excepted businesses, determined as set forth in this section, including detailed information for the different groups of assets identified in paragraphs (c)(5)(i) and (ii) and (d) of this section;

(*2*) The determination dates on which asset basis was measured during the taxable year;

(*3*) The names and taxpayer identification numbers (TINs) of all entities for which basis information is being provided, including partnerships and corporations if the taxpayer that owns an interest in a partnership or corporation looks through to the partnership's or corporation's basis in the partnership's or corporation's assets under paragraph (c)(5)(ii) of this section. If the taxpayer is a member of a consolidated group, the name and TIN of the agent for the group, as defined in § 1.1502–77, must be provided, but the taxpayer need not provide the names and TINs of all other consolidated group members;

(*4*) Asset basis information for corporations or partnerships if the taxpayer looks through to the corporation's or partnership's basis in the corporation's or partnership's assets under paragraph (c)(5)(ii) of this section;

(*5*) A summary of the method or methods used to determine asset basis in property used in both excepted and non-excepted businesses, as well as information regarding any deemed sale under paragraph (c)(5)(iv) of this section;

(*6*) Whether the taxpayer used the historical approach or the effective date approach for all of its disallowed disqualified interest; and

(*7*) If the taxpayer changed its methodology for allocating asset basis between or among two or more trades or businesses under paragraph (c)(3)(ii) of this section, a statement that the taxpayer has changed the allocation methodology and a description of the new methodology or, if the taxpayer is required to request consent for the allocation methodology change under paragraph (c)(3)(iii)(A)(*2*) of this section, a statement that the request has been or will be filed and a description of the methodology change.

(iv) *Failure to file statement.* If a taxpayer fails to file the statement described in paragraph (c)(6)(iii) of this section or files a statement that does not comply with the requirements of paragraph (c)(6)(iii) of this section, the Commissioner may treat the taxpayer as if all of its interest expense is properly allocable to a non-excepted trade or business, unless the taxpayer shows that there was reasonable cause for failing to comply with, and the taxpayer acted in good faith with respect to, the requirements of paragraph (c)(6)(iii) of this section, taking into account all pertinent facts and circumstances.

(7) *Ownership threshold for look-through rules*—(i) *Corporations*—(A) *Asset basis.* For purposes of this section, a shareholder must look through to the assets of a domestic non-consolidated C corporation or a relevant foreign corporation under paragraph (c)(5)(ii) of this section if the shareholder's direct and indirect interest in the corporation satisfies the ownership requirements of section 1504(a)(2). For purposes of this paragraph (c)(7)(i)(A), indirect stock ownership is determined by applying the constructive ownership rules of section 318(a). A shareholder may look through to the assets of an S corporation under paragraph (c)(5)(ii) of this section for purposes of allocating the shareholder's basis in its stock in the S corporation between excepted and non-excepted trades or businesses regardless of the shareholder's direct and indirect interest in the S corporation.

(B) *Dividends.* A shareholder must look through to the activities of a domestic non-consolidated C corporation or a relevant foreign corporation under paragraph (b)(3) of this section if the shareholder's direct interest in the corporation satisfies the ownership requirements of section 1504(a)(2). A shareholder may look through to the activities of a domestic non-consolidated C corporation or an applicable CFC under paragraph (b)(3) of this section if the shareholder's direct interest in the corporation is greater than or equal to 80 percent by value. A shareholder may look through to the activities of an S corporation under paragraph (b)(3) of this section regardless of the shareholder's direct interest in the S corporation.

(ii) *Partnerships.* A partner may look through to the assets of a partnership under paragraph (c)(5)(ii) of this section for purposes of allocating the partner's basis in its partnership interest between excepted and non-excepted trades or businesses regardless of the partner's direct and indirect interest in the partnership.

(iii) *Inapplicability of look-through rule.* For circumstances in which a taxpayer that satisfies the ownership threshold in this paragraph (c)(7) may not apply the look-through rules in paragraphs (b)(3) and (c)(5)(ii) of this section, see paragraph (c)(5)(ii)(D) of this section.

(8) *Anti-abuse rule.* If a principal purpose for the acquisition, disposition, or change in use of an asset was to artificially shift the amount of basis allocable to excepted or non-excepted trades or businesses on a determination date, the additional basis or change in use will not be taken into account for purposes of this section. For example, if an asset is used in a non-excepted trade or business for most of the taxable year, and if the taxpayer begins using the asset in an excepted trade or business towards the end of the year with a principal purpose of shifting the amount of basis in the asset that is allocable to the excepted trade or business, the change in use is disregarded for purposes of this section. A purpose may be a principal purpose even though it is outweighed by other purposes (taken together or separately). In determining whether a taxpayer has a principal purpose described in this paragraph (c)(8), factors to be considered include, for example, the following: The business purpose for the acquisition, disposition, or change in use; the length of time the asset was used in a trade or business; whether the asset was acquired from a related person; and whether the taxpayer's aggregate basis in its assets increased or decreased temporarily on or around a determination date. A principal purpose is presumed to be present in any case in which the acquisition, disposition, or change in use lacks a substantial business purpose and increases the taxpayer's basis in assets used in its excepted trades or businesses by more than 10 percent during the taxable year.

(d) *Direct allocations*—(1) *In general.* It is not necessary to allocate interest expense under this paragraph (d) if all of the taxpayer's interest expense is allocable to excepted trades or businesses or if all of the taxpayer's interest expense is allocable to non-excepted trades or businesses.

(2) *Qualified nonrecourse indebtedness.* For purposes of this section, a taxpayer with qualified nonrecourse indebtedness must directly allocate interest expense from the indebtedness to the taxpayer's assets in the manner and to the extent provided in § 1.861–10T(b). For purposes of this paragraph (d)(2), the term *qualified nonrecourse indebtedness* has the meaning provided in § 1.861–10T(b), except that the term *cash flow from the property* (within the meaning of § 1.861–10T(b)(3)(i)) includes revenue derived from the sale or lease of inventory or similar property with respect to an excepted regulated utility trade or business or a non-excepted regulated utility trade or business.

(3) *Assets used in more than one trade or business.* If an asset is used in more than one trade or business, the taxpayer must apply the rules in paragraph (c)(3) of this section to determine the extent to which interest that is directly allocated under this paragraph (d) is allocable to excepted or non-excepted trades or businesses.

(4) *Adjustments to basis of assets to account for direct allocations.* In determining the amount of a taxpayer's basis in the assets used in its excepted and non-excepted trades or businesses for purposes of paragraph (c) of this section, adjustments must be made to reflect direct allocations under this paragraph (d). These adjustments consist of reductions in the taxpayer's basis in its assets for purposes of paragraph (c) of this section to reflect assets to which interest expense is directly allocated under this paragraph (d). The amount of the taxpayer's basis in these assets must be reduced, but not below zero, by the amount of qualified nonrecourse indebtedness secured by these assets. These adjustments must be made before the taxpayer averages the adjusted basis in its assets as determined on each determination date during the taxable year.

(5) *Example: Direct allocation of interest expense*—(i) *Facts.* T conducts an electing real property trade or business (Business X) and operates a retail store that is a non-excepted trade or business (Business Y). In Year 1, T issues Note A to a third party in exchange for $1,000x for the purpose of acquiring Building B. Note A is qualified nonrecourse indebtedness (within the meaning of § 1.861–10T(b)) secured by Building B. T then uses those funds to acquire Building B for $1,200x, and T uses Building B in Business X. During Year 1, T pays $500x of interest, of which $100x is interest payments on Note A. For Year 1, T's basis in its assets used in Business X (as determined under paragraph (c) of this section) is $3,600x (excluding cash and cash equivalents), and T's basis in its assets used in Business Y (as determined under paragraph (c) of this section) is $800x (excluding cash and cash equivalents). Each of Business X and Business Y also has $100x of cash and cash equivalents.

(ii) *Analysis.* Because Note A is qualified nonrecourse indebtedness that is secured by Building B, in allocating interest expense between Businesses X and Y, T first must directly allocate the $100x of interest expense it paid with respect to Note A to Business X in accordance with paragraph (d)(2) of this section. Thereafter, T must allocate the remaining $400x of interest expense between Businesses X and Y under paragraph (c) of this section. After excluding $1,000x of T's basis in Building B to reflect the amount of Note A (see paragraph (d)(4) of this section), and without regard to T's $200x of cash and cash equivalents (see paragraph (c)(5)(iii) of this section), T's basis in its assets used in Businesses X and Y is $2,600x and $800x (76.5 percent and 23.5 percent), respectively. Thus, $306x of the remaining $400x of interest expense would be allocated to Business X, and $94x would be allocated to Business Y.

(e) *Examples.* The examples in this paragraph (e) illustrate the principles of this section. For purposes of these examples, no taxpayer is eligible for the small business exemption under section 163(j)(3) and § 1.163(j)–2(d), no taxpayer has floor plan financing interest expense, and no taxpayer has qualified nonrecourse indebtedness within the meaning of § 1.861–10T(b).

(1) *Example 1: Interest allocation within a consolidated group*—(i) *Facts.* S is a member of a consolidated group of which P is the common parent. P conducts an electing real property trade or business (Business X), and S conducts a non-excepted trade or business (Business Y). In Year 1, P pays or accrues (without regard to section 163(j)) $35x of interest expense and

receives $10x of interest income, and S pays or accrues (without regard to section 163(j)) $115x of interest expense and receives $5x of interest income (for a total of $150x of interest expense and $15x of interest income). For purposes of this example, assume that, pursuant to paragraph (c) of this section, $30x of the P group's interest expense and $3x of the P group's interest income is allocable to Business X, and the remaining $120x of interest expense and $12x of interest income is allocable to Business Y.

(ii) *Analysis.* Under paragraph (a)(4) of this section, 20 percent of the P group's Year 1 interest expense ($30x/$150x) and interest income ($3x/$15x) is allocable to an excepted trade or business. Thus, $7x ($35x × 20 percent) of P's interest expense and $2x ($10x × 20 percent) of P's interest income is allocable to an excepted trade or business. The remaining $28x of P's interest expense is business interest expense subject to the section 163(j) limitation, and the remaining $8x of P's interest income is business interest income that increases the group's section 163(j) limitation. In turn, $23x ($115x × 20 percent) of S's interest expense and $1x ($5x × 20 percent) of S's interest income is allocable to an excepted trade or business. The remaining $92x of S's interest expense is business interest expense subject to the section 163(j) limitation, and the remaining $4x of S's interest income is business interest income that increases the group's section 163(j) limitation.

(2) *Example 2: Interest allocation within a consolidated group with assets used in more than one trade or business*—(i) *Facts.* S is a member of a consolidated group of which P is the common parent. P conducts an electing real property trade or business (Business X), and S conducts a non-excepted trade or business (Business Y). In Year 1, P pays or accrues (without regard to section 163(j)) $50x of interest expense, and S pays or accrues $100x of interest expense (without regard to section 163(j)). P leases 40 percent of space in Building V (which P owns) to S for use in Business Y, and P leases the remaining 60 percent of space in Building V to third parties. For purposes of allocating interest expense under paragraph (c) of this section, the P group's basis in its assets (excluding Building V) used in Businesses X and Y is $180x and $620x, respectively. The P group's basis in Building V for purposes of allocating interest expense under paragraph (c) of this section is $200x.

(ii) *Analysis.* Under paragraph (c)(3)(ii) of this section, the P group's basis in Building V ($200x) is allocated to excepted and non-excepted trades or businesses in accordance with the use of space by Business Y (40 percent) and Business X (the remainder, or 60 percent). Accordingly, $120x of the basis in Building V is allocated to excepted trades or businesses (60 percent × $200x), and $80x is allocated to non-excepted trades or businesses (40 percent × $200x). After allocating the basis in Building V, the P group's total basis in the assets used in excepted and non-excepted trades or businesses is $300x and $700x, respectively. Under paragraphs (a)(4) and (c) of this section, 30 percent ($300x/$1,000x) of the P group's Year 1 interest expense is properly allocable to an excepted trade or business. Thus, $15x ($50x × 30 percent) of P's interest expense is properly allocable to an excepted trade or business, and the remaining $35x of P's interest expense is business interest expense subject to the section 163(j) limitation. In turn, $30x ($100x × 30 percent) of S's interest expense is properly allocable to an excepted trade or business, and the remaining $70x of S's interest expense is business interest expense subject to the section 163(j) limitation.

(3) *Example 3: Application of look-through rules*—(i) *Facts.* (A) Each of Corp A, Corp B, Corp C, and Corp D is a domestic calendar-year corporation that is not a member of a consolidated group. Corp A owns 100 percent of the stock of Corp C; the basis of Corp A's stock in Corp C is $500x. Corp C owns 10 percent of the interests in PS1 (a domestic partnership), and Corp B owns the remaining 90 percent. Corp C's basis in its PS1 interests is $25x; Corp B's basis in its PS1 interests is $225x. PS1 owns 100 percent of the stock of Corp D; the basis of PS1's stock in Corp D is $1,000x. Corp A and Corp B are owned by unrelated, non-overlapping shareholders.

(B) In 2021, Corp C was engaged solely in a non-excepted trade or business. That same year, PS1's only activity was holding Corp D stock. In turn, Corp D was engaged in both an electing farming business and a non-excepted trade or business. Under the allocation rules in paragraph (c) of this section, 50 percent of Corp D's asset basis in 2021 was allocable to the electing farming business, and the remaining 50 percent was allocable to the non-excepted trade or business.

(C) Corp A and Corp B each paid or accrued (without regard to section 163(j)) $150x of interest expense allocable to a trade or business. Corp A's trade or business was an excepted trade or business, and Corp B's trade or business was a non-excepted trade or business. Corp A's basis in the assets used in its trade or business was $100x, and Corp B's basis in the assets used in its trade or business was $112.5x.

(ii) *Analysis.* (A) As provided in paragraph (c)(5)(ii)(E) of this section, if a taxpayer applies the look-through rules of paragraph (c)(5)(ii) of this section, the taxpayer must begin with the lowest-tier entity to which it is eligible to apply the look-through rules. Corp A directly owns 100 percent of the stock of Corp C; thus, Corp A satisfies the 80 percent minimum ownership threshold with respect to Corp C. Corp A also owns 10 percent of the interests in PS1. There is no minimum ownership threshold for partnerships; thus, Corp A may apply the look-through rules to PS1. However, Corp A does not directly or indirectly own at least 80 percent of the stock of Corp D; thus, Corp A cannot look through its indirect interest in Corp D. In turn, Corp B directly owns 90 percent of the interests in PS1, and Corp B indirectly owns at least 80 percent of the stock of Corp D. Thus, Corp B must apply the look-through rules to PS1 and Corp D.

(B) From Corp A's perspective, PS1 is not engaged in a trade or business for purposes of section 163(j); instead, PS1 is merely holding its Corp D stock as an investment. Under paragraph (c)(5)(ii)(A)(*2*) of this section, if a partnership is not engaged in a trade or business, then its C corporation partner must treat its entire basis in the partnership interest as allocable to a non-excepted trade or business. Thus, for purposes of Corp A's application of the look-through rules, Corp C's entire basis in its PS1 interest ($25x) is allocable to a non-excepted trade or business. Corp C's basis in its other assets also is allocable to a non-excepted trade or business (the only trade or business in which Corp C is engaged). Thus, under paragraph (c) of this section, Corp A's $500x basis in its Corp C stock is allocable entirely to a non-excepted trade or business. Corp A's $100x basis in its other business assets is allocable to an excepted trade or business. Thus, 5⁄6 (or $125x) of Corp A's $150x of interest expense is properly allocable to a non-excepted trade or business and is business interest expense subject to the section 163(j) limitation, and the remaining $25x of Corp A's $150x of interest expense is allocable to an excepted trade or business and is not subject to the section 163(j) limitation.

(C) From Corp B's perspective, PS1 must look through its stock in Corp D to determine the extent to which PS1's basis in the stock is allocable to an excepted or non-excepted trade or business. Half of Corp D's basis in its assets is allocable to an excepted trade or business, and the other half is allocable to a non-excepted trade or business. Thus, from Corp B's perspective, $500x of PS1's basis in its Corp D stock (PS1's only asset) is allocable to an excepted trade or business, and the other half is allocable to a non-excepted trade or business. Corp B's basis in its PS1 interests is $225x. Applying the look-through rules to Corp B's PS1 interests, $112.5x of Corp B's basis in its PS1 interests is allocable to an excepted trade or business, and $112.5x of Corp B's basis in its PS1 interests is allocable to a non-excepted trade or business. Since Corp B's basis in the assets used in its non-excepted trade or business also was $112.5x, two-thirds of Corp B's interest expense ($100x) is properly allocable to a non-excepted trade or business and is business interest expense subject to the section 163(j) limitation, and one-third of Corp B's interest expense ($50x) is allocable to an excepted trade or business and is not subject to the section 163(j) limitation.

(4) *Example 4: Excepted and non-excepted trades or businesses in a consolidated group*—(i) *Facts.* P is the common parent of a consolidated group of which A and B are the only other members. A conducts an electing real property trade or business (Business X), and B conducts a non-excepted trade or business (Business Y). In Year 1, A pays or accrues (without regard to section 163(j)) $50x of interest expense and earns $70x of gross income in the conduct of Business X, and B pays or accrues (without regard to section 163(j)) $100x of interest expense and earns $150x of gross income in the conduct of Business Y. B owns Building V, which it uses in Business Y. For purposes of allocating the P group's Year 1 business interest expense between excepted and non-excepted trades or businesses under paragraph (c) of this section, the P group's basis in its assets (other than Building V) used in Businesses X and Y is $180x and $620x, respectively, and the P group's basis in Building V is $200x. At the end of Year 1, B sells Building V to a third party and realizes a gain of $60x in addition to the $150x of gross income B earned that year from the conduct of Business Y.

(ii) *Analysis.* (A) Under paragraphs (a)(4) and (c) of this section, the P group's basis in its assets used in its trades or businesses is allocated between the P group's excepted trade or business (Business X) and its non-excepted trade or business (Business Y) as though these trades or businesses were conducted by a single corporation. Under paragraph (c) of this section, the P group's basis in its assets used in Businesses X and Y is $180x and $820x, respectively. Accordingly, 18 percent ($180x/$1,000x) of the P group's total interest expense ($150x) is properly allocable to an excepted trade or business ($27x), and the remaining 82 percent of the P group's total interest expense is business interest expense properly allocable to a non-excepted trade or business ($123x).

(B) To determine the P group's section 163(j) limitation, paragraph (a) of this section requires that certain items of income and deduction be allocated to the excepted and non-excepted trades or businesses of the P group as though these trades or businesses were conducted by a single corporation. In Year 1, the P group's excepted trade or business (Business X) has gross income of $70x, and the P group's non-excepted trade or business (Business Y) has gross income of $150x. Because Building V was used exclusively in Business Y, the $60x of gain from the sale of Building V in Year 1 is attributed to Business Y under paragraph (b)(2) of this section. The P group's section 163(j) limitation is $63x (30 percent × $210x), which allows the P group to deduct $63x of its $123x of business interest expense allocated to the P group's non-excepted trades or businesses. The group's $27x of interest expense that is allocable to excepted trades or businesses may be deducted without limitation under section 163(j).

(iii) *Intercompany transaction.* The facts are the same as in *Example 4* in paragraph (e)(4)(i) of this section, except that A owns Building V and leases it to B in Year 1 for $20x for use in Business Y, and A sells Building V to a third party for a $60 gain at the end of Year 1. Under paragraphs (a)(4) and (c) of this section, all members of the P group are treated as a single corporation. As a result, the P group's basis in its assets used in its trades or businesses is allocated between the P group's excepted trade or business (Business X) and its non-excepted trade or business (Business Y) as though these trades or businesses were conducted by a single corporation. A lease between two divisions of a single corporation would produce no rental income or expense. Thus, the $20x of rent paid by B to A does not affect the P group's ATI. Moreover, under paragraph (c) of this section, Building V is an asset used in the P group's non-excepted trade or business (Business Y). Accordingly, although A owns Building V, the basis in Building V is added to the P group's basis in assets used in Business Y for purposes of allocating interest expense under paragraph (c) of this section. In the same vein, when A sells Building V to a third party at a gain of $60x, the gain is included in the P group's ATI because Building V was used in a non-excepted trade or business of the P group (Business Y) prior to its sale.

(5) *Example 5: Captive activities*—(i) *Facts.* S and T are members of a consolidated group of which P is the common parent. P conducts an electing real property trade or business (Business X), S conducts a non-excepted trade or business (Business Y), and T provides transportation services to Businesses X and Y but does not have any customers outside of the P group. For Year 1, T provides transportation services using a single bus with a basis of $120x.

(ii) *Analysis.* Under paragraph (a)(4) of this section, activities conducted by a consolidated group are treated as though those activities were conducted by a single corporation. Because the activities of T are limited to providing intercompany transportation services, T does not conduct a trade or business for purposes of section 163(j). Under paragraph (c)(3) of this section, business interest expense is allocated to excepted and non-excepted trades or businesses based on the relative basis of the assets used in those businesses. The basis in T's only asset, a bus, is therefore allocated between Business X and Business Y according to the use of T's bus by these businesses. Business X uses one-third of T's services, and Business Y uses two-thirds of T's services. Thus, $40x of the basis of T's bus is allocated to Business X, and $80x of the basis of T's bus is allocated to Business Y.

(6) *Example 6: Constructive ownership*—(i) *Facts.* P, S, T, and U are domestic C corporations that are not members of a consolidated group. P directly owns 80 percent of the stock of each of S and T as measured by total voting power and value; an unrelated third party, X, owns the remaining 20 percent. In turn, S and T directly own 15 percent and 80 percent, respectively, of the stock of U as measured by total voting power and value; P directly owns the remaining 5 percent. P conducts both excepted and non-excepted trades or businesses. S and T conduct only non-excepted trades or businesses, and U conducts both excepted and non-excepted trades or businesses.

(ii) *Analysis.* Under paragraph (c)(7)(i)(A) of this section, a shareholder must look through to the assets of a domestic non-consolidated C corporation for purposes of allocating the shareholder's basis in its stock in the corporation between excepted and non-excepted trades or businesses if the shareholder's direct and indirect interest in the corporation satisfies the ownership requirements of section 1504(a)(2). For purposes of paragraph (c)(7)(i)(A) of this section, a shareholder's stock ownership is determined by applying the constructive ownership rules of section 318(a). P directly owns 80 percent of each of S and T as measured by total voting power and value; thus, P must look through to the assets of S and T when allocating the basis in its stock of S and T. P directly owns 5 percent of the stock of U as measured by total voting power and value, and P constructively owns the other 95 percent; thus, P also must look through to U's assets when allocating the basis in its U stock. S directly owns 15 percent of the stock of U, and S constructively owns only 5 percent through P; thus, S cannot look through to U's assets when allocating the basis in its U stock. T directly owns 80 percent of the stock of U, and T constructively owns an additional 5 percent; thus, T must look through to U's assets when allocating the basis in its U stock.

(iii) *Dividend.* The facts are the same as in paragraph (e)(6)(i) of this section, except that U distributes a $160x dividend pro rata to its shareholders. Thus, P receives $8x (5 percent of $160x) of the U dividend, S receives $24x (15 percent of $160x), and T receives $128x (80 percent of $160x). Under paragraph (c)(7)(i)(B) of this section, if a shareholder's direct interest in a corporation satisfies the ownership requirements of section 1504(a)(2), the shareholder must look through to the activities of a domestic non-consolidated C corporation in determining whether dividend income is from an excepted or non-excepted trade or business. The constructive ownership rules do not apply in allocating dividends under paragraph (c)(7)(i)(B) of this section. P directly owns 5 percent of the stock of U as measured by vote and value, and S directly owns 15 percent of the stock of U as measured by vote and value; thus, neither P nor S is required to apply the look-through rules in allocating its dividend income from U, and all such income is allocable to non-excepted trades or businesses. T directly owns 80 percent of the stock of U as measured by vote and value; thus, T must allocate its U dividend in accordance with the activities of U's excepted and non-excepted trades or businesses.

(7) *Example 7: Dispositions with a principal purpose of shifting basis*—(i) *Facts.* U and V are members of a consolidated group of which P is the common parent. U conducts an electing farming business (Business F), and V conducts a farm equipment leasing business (Business L) that is a non-excepted trade or business. After the end of a farming season, the P group, with a principal purpose of shifting basis from Business L to Business F, has V sell to U all off-lease farming equipment that previously was leased out as part of Business L. Immediately before the start of the next season, U sells the farming equipment back to V for use in Business L.

(ii) *Analysis.* Under paragraph (c)(8) of this section, in the case of a disposition of assets undertaken with a principal purpose of artificially shifting the amount of basis allocable to excepted or non-excepted trades or businesses on a determination date, the additional basis or change in use will not be taken into account. Because V's sale of farming equipment to U for storage in Business F's facilities is undertaken with a principal purpose of shifting basis from Business L to Business F, the additional basis Business F receives from these transactions will not be taken into account for purposes of this section. Instead, the basis of the farming equipment will be allocated as though the farming equipment continued to be used in Business L.

(f) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year. Accordingly, for purposes of § 1.163(j)–10(c)(5), taxpayers make any change to the alternative depreciation system as of November 13, 2020, or if relying on the provisions of § 1.163(j)–10 in regulation project REG–106089–18 (83 FR 67490), as of December 28, 2018.

§ 1.163(j)–11 Transition rules.

(a) *Overview.* This section provides transition rules regarding the section 163(j) limitation. Paragraph (b) of this section provides rules regarding the application of the section 163(j) limitation to a corporation that joins a consolidated group during a taxable year of the group beginning before January 1, 2018 and is subject to the section 163(j) limitation at the time of its change in status. Paragraph (c) of this section provides rules regarding the treatment of carryforwards of disallowed disqualified interest.

(b) *Application of section 163(j) limitation if a corporation joins a consolidated group during a taxable year of the group beginning before January 1, 2018*—(1) *In general.* If a corporation (S) joins a consolidated group during a taxable year of the group beginning before January 1, 2018, and if S is subject to the section 163(j) limitation at the time of its change in status, then section 163(j) will apply to S's short taxable year that ends on the day of S's change in status, but section 163(j) will not apply to S's short taxable year that begins the next day (when S is a member of the acquiring consolidated group). Any business interest expense paid or accrued (without regard to section 163(j)) by S in its short taxable year ending on the day of S's change in status for which a deduction is disallowed under section 163(j) will be carried forward to the acquiring group's first taxable year beginning after December 31, 2017. Those disallowed business interest expense carryforwards may be subject to limitation under other provisions of these regulations (see, for example, § 1.163(j)–5(c), (d), (e), and (f)).

(2) *Example.* Acquiring Group is a consolidated group with a fiscal year end of November 30; Target is a stand-alone calendar-year C corporation. On May 31, 2018, Acquiring Group acquires Target in a transaction that is not an ownership change for purposes of section 382. Acquiring Group is not subject to the section 163(j) limitation during its taxable year beginning December 1, 2017. As a result of the acquisition, Target has a short taxable year beginning January 1, 2018 and ending May 31, 2018. Target is subject to the section 163(j) limitation during this short taxable year. However, Target (as a member of Acquiring Group) is not subject to the section 163(j) limitation during Acquiring Group's taxable year ending November 30, 2018. Any disallowed business interest expense carryforwards from Target's taxable year ending May 31, 2018, will not be available for use in Acquiring Group's taxable year ending November 30, 2018. However, that disallowed business interest expense is carried forward to Acquiring Group's taxable year beginning December 1, 2018, and can be deducted by the group, subject to the

separate return limitation year (SRLY) limitation. See § 1.163(j)–5(d).

(c) *Treatment of disallowed disqualified interest*—(1) *In general.* Disallowed disqualified interest is carried forward to the taxpayer's first taxable year beginning after December 31, 2017. Disallowed disqualified interest is subject to disallowance as a disallowed business interest expense carryforward under section 163(j) and § 1.163(j)–2 to the extent the interest is properly allocable to a non-excepted trade or business under § 1.163(j)–10. Disallowed disqualified interest that is properly allocable to an excepted trade or business is not subject to the section 163(j) limitation. See § 1.163(j)–10(a)(6) for rules governing the allocation of disallowed disqualified interest between excepted and non-excepted trades or businesses.

(2) *Earnings and profits.* A taxpayer may not reduce its earnings and profits in a taxable year beginning after December 31, 2017, to reflect any disallowed disqualified interest carryforwards to the extent the payment or accrual of the disallowed disqualified interest reduced the earnings and profits of the taxpayer in a prior taxable year.

(3) *Disallowed disqualified interest of members of an affiliated group*—(i) *Scope.* This paragraph (c)(3)(i) applies to corporations that were treated as a single taxpayer under old section 163(j)(6)(C) and that had disallowed disqualified interest.

(ii) *Allocation of disallowed disqualified interest to members of the affiliated group*—(A) *In general.* Each member of the affiliated group is allocated its allocable share of the affiliated group's disallowed disqualified interest as provided in paragraph (c)(3)(ii)(B) of this section.

(B) *Definitions.* The following definitions apply for purposes of paragraph (c)(3)(ii) of this section.

(*1*) *Allocable share of the affiliated group's disallowed disqualified interest.* The term *allocable share of the affiliated group's disallowed disqualified interest* means, with respect to any member of an affiliated group for the member's last taxable year beginning before January 1, 2018, the product of the total amount of the disallowed disqualified interest of all members of the affiliated group under old section 163(j)(6)(C) and the member's disallowed disqualified interest ratio.

(*2*) *Disallowed disqualified interest ratio.* The term *disallowed disqualified interest ratio* means, with respect to any member of an affiliated group for the member's last taxable year beginning before January 1, 2018, the ratio of the exempt related person interest expense of the member for the last taxable year beginning before January 1, 2018, to the sum of the amounts of exempt related person interest expense for all members of the affiliated group.

(*3*) *Exempt related person interest expense.* The term *exempt related person interest expense* means interest expense that is, or is treated as, paid or accrued by a domestic C corporation, or by a foreign corporation with income, gain, or loss that is effectively connected, or treated as effectively connected, with the conduct of a trade or business in the United States, to—

(*i*) Any person related to the taxpayer, within the meaning of sections 267(b) or 707(b)(1), applying the constructive ownership and attribution rules of section 267(c), if no U.S. tax is imposed with respect to the interest under subtitle A of the Code, determined without regard to net operating losses or net operating loss carryovers, and taking into account any applicable treaty obligation of the United States. For this purpose, interest that is subject to a reduced rate of tax under any treaty obligation of the United States applicable to the recipient is treated as, in part, subject to the statutory tax rate under sections 871 or 881 and, in part, not subject to tax, based on the proportion that the rate of tax under the treaty bears to the statutory tax rate. Thus, for purposes of section 163(j), if the statutory tax rate is 30 percent, and pursuant to a treaty U.S. tax is instead limited to a rate of 10 percent, two-thirds of the interest is considered interest not subject to U.S. tax under subtitle A of the Code;

(*ii*) A person that is not related to the taxpayer, within the meaning of section 267(b) or 707(b)(1), applying the constructive ownership and attribution rules of section 267(c), with respect to indebtedness on which there is a disqualified guarantee, within the meaning of paragraph (6)(D) of old section 163(j), of such indebtedness, and no gross basis U.S. tax is imposed with respect to the interest. For purposes of this paragraph (c)(3)(ii)(B)(*3*)(*ii*), a *gross basis U.S. tax* means any tax imposed by this subtitle A of the Code that is determined by reference to the gross amount of any item of income without any reduction for any deduction allowed by subtitle A of the Code. Interest that is subject to a gross basis U.S. tax that is eligible for a reduced rate of tax under any treaty obligation of the United States applicable to the recipient is treated as, in part, subject to the statutory tax rate under section 871 or 881 and, in part, not subject to a gross basis U.S. tax, based on the proportion that the rate of tax under the treaty bears to the statutory tax rate. Thus, for purposes of section 163(j), if the statutory tax rate is 30 percent, and pursuant to a treaty U.S. tax is instead limited to a rate of 10 percent, two-thirds of the interest is considered interest not subject to a gross basis U.S. tax under subtitle A of the Code; or

(*iii*) A REIT, directly or indirectly, to the extent that the domestic C corporation, or a foreign corporation with income, gain, or loss that is effectively connected, or treated as effectively connected, with the conduct of a trade or business in the United States, is a taxable REIT subsidiary, as defined in section 856(l), with respect to the REIT.

(iii) *Treatment of carryforwards.* The amount of disallowed disqualified interest allocated to a taxpayer pursuant to paragraph (c)(3)(ii) of this section is treated in the same manner as described in paragraph (c)(1) of this section.

(4) *Application of section 382*—(i) *Ownership change occurring before* November 13, 2020—(A) *Pre-change loss.* For purposes of section 382(d)(3), unless the rules of § 1.382–2(a)(7) apply, disallowed disqualified interest is not a pre-change loss under § 1.382–2(a) subject to a section 382 limitation with regard to an ownership change on a change date occurring before November 13, 2020. But see section 382(h)(6)(B) (regarding built-in deduction items).

(B) *Loss corporation.* For purposes of section 382(k)(1), unless the rules of § 1.382–2(a)(7) apply, disallowed disqualified interest is not a carryforward of disallowed interest described in section 381(c)(20) with regard to an ownership change on a change date occurring before November 13, 2020. But see section 382(h)(6) (regarding built-in deductions).

(ii) *Ownership change occurring on or after* November 13, 2020—(A) *Pre-change loss.* For rules governing the treatment of disallowed disqualified interest as a pre-change loss for purposes of section 382 with regard to an ownership change on a change date occurring on or after November 13, 2020, see §§ 1.382–2(a)(2) and 1.382–6(c)(3).

(B) *Loss corporation.* For rules governing when disallowed disqualified interest causes a corporation to be a loss corporation with regard to an ownership change occurring on or after November 13, 2020, see § 1.382–2(a)(1)(i)(A).

(5) *Treatment of excess limitation from taxable years beginning before January 1, 2018.* No amount of excess limitation under old section 163(j)(2)(B) may be carried forward to taxable years beginning after December 31, 2017.

(6) *Example: Members of an affiliated group*—(i) *Facts.* A, B, and C are calendar-year domestic C corporations that are members of an affiliated group (within the meaning of section 1504(a)) that was treated as a single taxpayer under old section 163(j)(6)(C) and the proposed regulations in this part under old section 163(j) (see formerly proposed § 1.163(j)–5). For the taxable year ending December 31, 2017, the separately determined amounts of exempt related person interest expense of A, B, and C were $0, $600x, and $150x, respectively (for a total of $750x). The affiliated group has $200x of disallowed disqualified interest in that year.

(ii) *Analysis.* The affiliated group's disallowed disqualified interest expense for the 2017 taxable year ($200x) is allocated among A, B, and C based on the ratio of each member's exempt related person interest expense to the group's exempt related person interest expense. Because A has no exempt related person interest expense, no disallowed disqualified interest is allocated to A. Disallowed disqualified interest of $160x is allocated to B (($600x/$750x) × $200x), and disallowed disqualified interest of $40x is allocated to C (($150x/$750x) × $200x). Thus, B and C have $160x and $40x, respectively, of disallowed disqualified interest that is carried forward to the first taxable year beginning after December 31, 2017. No excess limitation that was allocated to A, B, or C under old section 163(j) will carry forward to a taxable year beginning after December 31, 2017.

(iii) *Carryforward of disallowed disqualified interest to 2018 taxable year.* The facts are the same as in the *Example* in paragraph (c)(7)(i) of this section, except that, for the taxable year ending December 31, 2018, A, B, and C are members of a consolidated group that has a section 163(j) limitation of $140x, current-year business interest expense (as defined in § 1.163(j)–1(b)(9)) of $80x, and no excepted trade or business. Under paragraph (c)(1) of this section, disallowed disqualified interest is carried to the taxpayer's first taxable year beginning after December 31, 2017, and is subject to disallowance under section 163(j) and § 1.163(j)–2. Under § 1.163(j)–5(b)(3)(ii)(D)(*1*), a consolidated group that has section 163(j) limitation remaining for the current year after deducting all current-year business interest expense deducts each member's disallowed disqualified interest carryforwards from prior taxable years, starting with the earliest taxable year, on a pro rata basis (subject to certain limitations). In accordance with paragraph (c)(1) of this section, the rule in § 1.163(j)–5(b)(3)(ii)(D)(*1*) applies to disallowed disqualified interest carried forward to the taxpayer's first taxable year beginning after December 31, 2017. Accordingly, after deducting $80x of current-year business interest expense in 2018, the group may deduct $60x of its $200x disallowed disqualified interest carryforwards. Under paragraph (c)(3) of this section, B has $160x of disallowed disqualified interest carryforwards, and C has $40x of disallowed disqualified interest carryforwards. Thus, $48x (($160x/$200x) × $60x) of B's disallowed disqualified interest carryforwards, and $12x (($40x/$200x) × $60x) of C's disallowed disqualified interest carryforwards, are deducted by the consolidated group in the 2018 taxable year.

(d) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

■ **Par. 4.** Section 1.263A–9 is amended by revising the first and third sentences of paragraph (g)(1)(i) to read as follows:

§ 1.263A–9 The avoided cost method.

* * * * *

(g) * * *

(1) * * *

(i) * * * Interest must be capitalized under section 263A(f) before the application of section 163(d) (regarding the investment interest limitation), section 163(j) (regarding the limitation on business interest expense), section 266 (regarding the election to capitalize carrying charges), section 469 (regarding the limitation on passive losses), and section 861 (regarding the allocation of interest to United States sources). * * * However, in applying section 263A(f) with respect to the excess expenditure amount, the taxpayer must capitalize all interest that is neither investment interest under section 163(d), business interest expense under section 163(j), nor passive interest under section 469 before capitalizing any interest that is either investment interest, business interest expense, or passive interest. * * *

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■ **Par. 5.** Section 1.263A–15 is amended by adding paragraph (a)(4) to read as follows:

§ 1.263A–15 Effective dates, transitional rules, and anti-abuse rules.

(a) * * *

(4) Section 1.263A–9(g)(1)(i) applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of that section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), and, if applicable, §§ 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

* * * * *

■ **Par. 6.** Section 1.381(c)(20)–1 is added to read as follows:

§ 1.381(c)(20)–1 Carryforward of disallowed business interest.

(a) *Carryover requirement.* Section 381(c)(20) provides that the acquiring corporation in a transaction described in section 381(a) will succeed to and take into account the carryover of disallowed business interest described in section 163(j)(2) to taxable years ending after the date of distribution or transfer.

(b) *Carryover of disallowed business interest described in section 163(j)(2).* For purposes of section 381(c)(20) and this section, the term *carryover of disallowed business interest described in section 163(j)(2)* means the disallowed business interest expense carryforward (as defined in § 1.163(j)–1(b)(11)), including any disallowed disqualified interest (as defined in § 1.163(j)–1(b)(12)), and including the distributor or transferor corporation's disallowed business interest expense from the taxable year that ends on the date of distribution or transfer. For the application of section 382 to disallowed business interest expense described in section 163(j)(2), see the regulations in this part under section 382 of the Code, including but not limited to § 1.382–2.

(c) *Limitation on use of disallowed business interest expense carryforwards in the acquiring corporation's first taxable year ending after the date of distribution or transfer*—(1) *In general.* In determining the extent to which the acquiring corporation may use disallowed business interest expense carryforwards in its first taxable year ending after the date of distribution or transfer, the principles of §§ 1.381(c)(1)–1 and 1.381(c)(1)–2 apply with appropriate adjustments, including but not limited to the adjustments described in paragraphs (c)(2) and (3) of this section.

(2) *One date of distribution or transfer within the acquiring corporation's taxable year.* If the acquiring corporation succeeds to the disallowed business interest expense carryforwards of one or more distributor or transferor corporations on a single date of distribution or transfer within one taxable year of the acquiring corporation, then, for the acquiring corporation's first taxable year ending after the date of distribution or transfer, that part of the acquiring corporation's business interest expense deduction (if any) that is attributable to the disallowed business interest expense carryforwards of the distributor or transferor corporation is limited under this paragraph (c) to an amount equal to the post-acquisition portion of the acquiring corporation's section 163(j) limitation, as defined in paragraph (c)(4) of this section.

(3) *Two or more dates of distribution or transfer in the taxable year.* If the acquiring corporation succeeds to the disallowed business interest expense carryforwards of two or more distributor or transferor corporations on two or more dates of distribution or transfer within one taxable year of the acquiring corporation, the limitation to be applied under this paragraph (c) is determined by applying the principles of § 1.381(c)(1)–2(b) to the post-acquisition portion of the acquiring corporation's section 163(j) limitation, as defined in paragraph (c)(4) of this section.

(4) *Definition.* For purposes of this paragraph (c), the term *post-acquisition portion of the acquiring corporation's section 163(j) limitation* means the amount that bears the same ratio to the acquiring corporation's section 163(j) limitation (within the meaning of § 1.163(j)–1(b)(31)) (or, if the acquiring corporation is a member of a consolidated group, the consolidated group's section 163(j) limitation) for the first taxable year ending after the date of distribution or transfer (taking into account items to which the acquiring corporation succeeds under section 381, other than disallowed business interest expense carryforwards) as the number of days in that year after the date of distribution or transfer bears to the total number of days in that year.

(5) *Examples.* For purposes of this paragraph (c)(5), unless otherwise stated, X, Y, and Z are taxable domestic C corporations that were incorporated on January 1, 2021 and that file their tax returns on a calendar-year basis; none of X, Y, or Z is a member of a consolidated group; the small business exemption in § 1.163(j)–2(d) does not apply; interest expense is deductible except to the extent of the potential application of section 163(j); and the facts set forth the only corporate activity. The principles of this paragraph (c) are illustrated by the following examples.

(i) *Example 1: Transfer before last day of acquiring corporation's taxable year*—(A) *Facts.* On October 31, 2022, X transferred all of its assets to Y in a statutory merger to which section 361 applies. For the 2021 taxable year, X had $400x of disallowed business interest expense, and Y had $0 of disallowed business interest expense. For the taxable year ending October 31, 2022, X had an additional $350x of disallowed business interest expense (X did not deduct any of its 2021 carryforwards in its 2022 taxable year). For the taxable year ending December 31, 2022, Y had business interest expense of $100x, business interest income of $200x, and ATI of $1,000x. Y's section 163(j) limitation for the 2022 taxable year was $500x ($200x + (30 percent × $1,000x) = $500x).

(B) *Analysis.* Pursuant to § 1.163(j)–5(b)(2), Y deducts its $100x of current-year business interest expense (as defined in § 1.163(j)–1(b)(9)) before any disallowed business interest expense carryforwards (including X's carryforwards) from a prior taxable year are deducted. The aggregate disallowed business interest expense of X carried forward under section 381(c)(20) to Y's taxable year ending December 31, 2022, is $750x. However, pursuant to paragraph (c)(2) of this section, for Y's first taxable year ending after the date of distribution or transfer, the maximum amount of X's disallowed business interest expense carryforwards that Y can deduct is equal to the post-acquisition portion of Y's section 163(j) limitation. Pursuant to paragraph (c)(4) of this section, the post-acquisition portion of Y's section 163(j) limitation means Y's section 163(j) limitation times the ratio of the number of days in the taxable year after the date of distribution or transfer to the total number of days in that year. Therefore, only $84x of the aggregate amount ($500x × (61/365) = $84x) may be deducted by Y in that year, and the remaining $666x ($750x − $84x = $666x) is carried forward to the succeeding taxable year.

(C) *Transfer on last day of acquiring corporation's taxable year.* The facts are the same as in *Example 1* in paragraph (c)(5)(i)(A) of this section, except that X's transfer of its assets to Y occurred on December 31, 2022. For the taxable year ending December 31, 2022, X had an additional $350x of disallowed business interest expense (X did not deduct any of its 2021 carryforwards in its 2022 taxable year). For the taxable year ending December 31, 2023, Y had business interest expense of $100x, business interest income of $200x, and ATI of $1,000x. Y's section 163(j) limitation for the 2023 taxable year was $500x ($200x + (30 percent × $1,000x) = $500x). The aggregate disallowed business interest expense of X carried under section 381(c)(20) to Y's taxable year ending December 31, 2023, is $750x. Paragraph (c)(2) of this section does not limit the amount of X's disallowed business interest expense carryforwards that may be deducted by Y in the 2023 taxable year. Since the amount of Y's section 163(j) limit for the 2023 taxable year was $500x, Y may deduct the full amount ($100x) of its own business interest expense for the 2023 taxable year, along with $400x of X's disallowed business interest expense carryforwards.

(ii) *Example 2: Multiple transferors on same date*—(A) *Facts.* On October 31, 2022, X and Y transferred all of their assets to Z in statutory mergers to which section 361 applies. For the 2021 taxable year, X had $300x of disallowed business interest expense, Y had $200x, and Z had $0. For the taxable year ending October 31, 2022, each of X and Y had an additional $125x of disallowed business interest expense (neither X nor Y deducted any of its 2021 carryforwards in 2022). For the taxable year ending December 31, 2022, Z had business interest expense of $100x, business interest income of $200x, and ATI of $1,000x. Z's section 163(j) limitation for the 2022 taxable year was $500x ($200x + (30 percent × $1,000x) = $500x).

(B) *Analysis.* The aggregate disallowed business interest expense of X and Y carried under section 381(c)(20) to Z's taxable year ending December 31, 2022, is $750x. However, pursuant to paragraph (c)(2) of this section, only $84x of the aggregate amount ($500x × (61/365) = $84x) may be deducted by Z in that year. Moreover, under paragraph (b)(2) of this section, this amount only may be deducted by Z in that year after

Z has deducted its $100x of current-year business interest expense (as defined in § 1.163(j)–1(b)(9)).

(d) *Applicability date.* This section applies to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to ta axable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), and, if applicable, §§ 1.263A–9, 1.263A–15, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

■ **Par. 7.** Section 1.382–1 is amended by:

■ 1. Adding an entry for § 1.382–2(a)(1)(vi) and (a)(7) and (8);

■ 2. Revising the entry for § 1.382–2(b)(3);

■ 3. Adding entries for § 1.382–6(a)(1) and (2) and (b)(4);

■ 4. Revising the entry for § 1.382–6(h); and

■ 5. Adding an entry for § 1.382–7(c), (d), (d)(1) through (5), (e) through (g), and (g)(1) through (4).

The additions and revisions read as follows:

§ 1.382–1 Table of contents.

* * * * *

§ 1.382–2 General rules for ownership change.

(a) * * *

(1) * * *

(vi) Any section 382 disallowed business interest carryforward.

* * * * *

(7) Section 382 disallowed business interest carryforward.

(8) Testing period.

(b) * * *

(3) Rules provided in paragraphs (a)(1)(i)(A), (a)(1)(ii), (iv), and (v), (a)(2)(iv) through (vi), (a)(3)(i), and (a)(4) through (8) of this section.

* * * * *

§ 1.382–6 Allocation of income and loss to periods before and after the change date for purposes of section 382.

(a) * * *

(1) In general.

(2) Allocation of business interest expense.

(i) Scope.

(ii) Deductibility of business interest expense.

* * * * *

(b) * * *

(4) Allocation of business interest expense.

(i) Scope.

(ii) Deductibility of business interest expense.

(iii) Example.

* * * * *

(h) Applicability date.

(1) In general.

(2) Paragraphs (a) and (b)(1) and (4) of this section.

* * * * *

§ 1.382–7

* * * * *

(c) [Reserved]

(d) *Special rules.*

(1)–(4) [Reserved]

(5) Section 382 disallowed business interest carryforwards.

(e)–(f) [Reserved]

(g) *Applicability dates.*

(1)–(3) [Reserved]

(4) Paragraph (d)(5) of this section.

* * * * *

■ **Par. 8.** Section 1.382–2 is amended by:

■ 1. Revising paragraph (a)(1)(i)(A);

■ 2. Removing '', or'' and adding ''; or'' in its place at the end of paragraph (a)(1)(i)(B);

■ 3. Revising paragraphs (a)(1)(ii) introductory text and (a)(1)(ii)(A);

■ 4. Removing '', and'' and adding ''; and'' in its place at the end of paragraph (a)(1)(ii)(B);

■ 5. Removing the last sentence in paragraphs (a)(1)(iv) and (v);

■ 6. Removing the commas and adding semicolons in their place at the end of paragraphs (a)(2)(i) and (iii);

■ 7. Removing the period and adding a semicolon in its place at the end of paragraph (a)(2)(ii);

■ 8. Removing '', and'' and adding a semicolon in its place at the end of paragraph (a)(2)(iv);

■ 9. Removing the period and adding ''; and'' in its place at the end of paragraph (a)(2)(v);

■ 10. Adding paragraph (a)(2)(vi);

■ 11. Removing the last sentence in paragraphs (a)(3)(i), (a)(4)(i), and (a)(5) and (6);

■ 12. Adding paragraphs (a)(7) and (8); and

■ 13. Revising paragraph (b)(3).

The revisions and additions read as follows:

§ 1.382–2 General rules for ownership change.

(a) * * *

(1) * * *

(i) * * *

(A) Is entitled to use a net operating loss carryforward, a capital loss carryover, a carryover of excess foreign taxes under section 904(c), a carryforward of a general business credit under section 39, a carryover of a minimum tax credit under section 53, or a section 382 disallowed business interest carryforward described in paragraph (a)(7) of this section;

* * * * *

(ii) *Distributor or transferor loss corporation in a transaction under section 381.* Notwithstanding that a loss corporation ceases to exist under state law, if its disallowed business interest expense carryforwards, net operating loss carryforwards, excess foreign taxes, or other items described in section 381(c) are succeeded to and taken into account by an acquiring corporation in a transaction described in section 381(a), such loss corporation will be treated as continuing in existence until—

(A) Any pre-change losses (excluding pre-change credits described in § 1.383–1(c)(3)), determined as if the date of such transaction were the change date, are fully utilized or expire under section 163(j), 172, or 1212;

* * * * *

(2) * * *

(vi) Any section 382 disallowed business interest carryforward.

* * * * *

(7) *Section 382 disallowed business interest carryforward.* The term *section 382 disallowed business interest carryforward* includes the following items:

(i) The loss corporation's disallowed business interest expense carryforwards (as defined in § 1.163(j)–1(b)(11)), including disallowed disqualified interest (as defined in § 1.163(j)–1(b)(12)), as of the date of the ownership change.

(ii) The loss corporation's current-year business interest expense (as defined in § 1.163(j)–1(b)(9)) in the change year (as defined in § 1.382–6(g)(1)) that is allocable to the pre-change period (as defined in § 1.382–6(g)(2)) under § 1.382–6(a) or (b) and that becomes disallowed business interest expense (as defined in § 1.163(j)–1(b)(10)).

(8) *Testing period.* Notwithstanding the temporal limitations provided in § 1.382–2T(d)(3)(i), the testing period for a loss corporation can begin as early as the first day of the first taxable year from which there is a section 382 disallowed business interest carryforward to the first taxable year ending after the testing date.

(b) * * *

(3) *Rules provided in paragraphs (a)(1)(i)(A), (a)(1)(ii), (iv), and (v), (a)(2)(iv) through (vi), (a)(3)(i), and (a)(4) through (8) of this section.* The rules provided in paragraphs (a)(1)(i)(A), (a)(1)(ii), (iv), and (v), (a)(2)(iv) through (vi), (a)(3)(i), and (a)(4) through (8) of this section apply to testing dates

occurring on or after November 13, 2020. For loss corporations that have testing dates occurring before November 13, 2020, see § 1.382–2 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to testing dates occurring during a taxable year beginning after December 31, 2017, and before November 13, 2020, so long as the taxpayers and their related parties consistently apply the rules of this section, the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), §§ 1.382–1, 1.382–5, 1.382–6, 1.382–7, 1.383–0, and 1.383–1, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

■ **Par. 9.** Section 1.382–5 is amended by revising the first and second sentences of paragraph (d)(1) and by adding three sentences to the end of paragraph (f) to read as follows:

§ 1.382–5 Section 382 limitation.

* * * * *

(d) * * *

(1) * * * If a loss corporation has two (or more) ownership changes, any losses or section 382 disallowed business interest carryforwards ((within the meaning of § 1.382–2(a)(7)) attributable to the period preceding the earlier ownership change are treated as pre-change losses with respect to both ownership changes. Thus, the later ownership change may result in a lesser (but never in a greater) section 382 limitation with respect to such pre-change losses. * * *

* * * * *

(f) * * * Paragraph (d)(1) of this section applies with respect to an ownership change occurring on or after November 13, 2020. For loss corporations that have undergone an ownership change before or after November 13, 2020, see § 1.382–5 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to testing dates occurring during a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of this section, the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), §§ 1.382–1, 1.382–2, 1.382–6, 1.382–7, 1.383–0, and 1.383–1, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year.

■ **Par. 10.** Section 1.382–6 is amended by:

■ 1. Redesignating the text of paragraph (a) as paragraph (a)(1);

■ 2. Adding a subject heading to newly redesignated paragraph (a)(1);

■ 3. Adding paragraph (a)(2);

■ 4. Removing the language ''Subject to paragraphs (b)(3)(ii) and (d)'' in the first sentence of paragraph (b)(1) and adding ''Subject to paragraphs (b)(3)(ii), (b)(4), and (d)'' in its place;

■ 5. Adding paragraph (b)(4); and

■ 6. Revising paragraph (h).

The additions and revision read as follows:

§ 1.382–6 Allocation of income and loss to periods before and after the change date for purposes of section 382.

(a) * * *

(1) *In general.* * * *

(2) *Allocation of business interest expense*—(i) *Scope.* Except as provided in paragraph (b)(4) of this section, this paragraph (a)(2) applies if a loss corporation has business interest expense (as defined in § 1.163(j)–1(b)(3)) in the change year. The rules of this paragraph (a)(2) apply to determine the amount of current-year business interest expense (as defined in § 1.163(j)–1(b)(9)) that is deducted in the change year. These rules also apply to determine the amount of any current-year business interest expense that is characterized as disallowed business interest expense (as defined in § 1.163(j)–1(b)(10)) allocable to the pre-change period and the post-change period, and to allocate disallowed business interest expense carryforwards (as defined in § 1.163(j)–1(b)(11)) to the change year for deduction in the pre-change period and the post-change period.

(ii) *Deductibility of business interest expense.* The rules of this paragraph (a)(2)(ii) apply in the following order.

(A) First, the loss corporation calculates its section 163(j) limitation (as defined in § 1.163(j)–1(b)(36)) for the change year.

(B) Second, the loss corporation calculates its deductible current-year BIE and deducts this amount in determining its taxable income or net operating loss for the change year. For purposes of this paragraph (a)(2)(ii), the term *deductible current-year BIE* means the loss corporation's current-year business interest expense (including its floor plan financing interest expense, as defined in § 1.163(j)–1(b)(19)), to the extent of its section 163(j) limitation.

(C) Third, if the loss corporation has disallowed business interest expense paid or accrued (without regard to section 163(j)) in the change year that is carried forward to post-change years, it allocates an equal portion of that disallowed business interest expense to each day in the change year. Any amount of disallowed business interest expense that is allocated to the pre-change period pursuant to this paragraph (a)(2)(ii)(C) is carried forward subject to section 382(d)(3). Any amount of disallowed business interest expense that is allocated to the post-change period pursuant to this paragraph (a)(2)(ii)(C) is carried forward and is not subject to section 382(d)(3).

(D) Fourth, if the loss corporation has excess section 163(j) limitation, then the loss corporation calculates its deductible disallowed business interest expense carryforward and allocates an equal portion to each day in the change year. For purposes of this paragraph (a)(2)(ii), the term *excess section 163(j) limitation* means the excess, if any, of the loss corporation's section 163(j) limitation over its deductible current-year BIE, and the term *deductible disallowed business interest expense carryforward* means the loss corporation's disallowed business interest expense carryforward to the extent of its excess section 163(j) limitation.

(E) Fifth, the loss corporation deducts its deductible disallowed business interest expense carryforward that was allocated to the pre-change period under paragraph (a)(2)(ii)(D) of this section. Subject to the application of sections 382(b)(3)(B) and 382(d)(3), the loss corporation deducts its deductible disallowed business interest expense carryforward that was allocated to the post-change period under paragraph (a)(2)(ii)(D) of this section. Any amount of disallowed business interest expense carryforward that is not deducted pursuant to this paragraph (a)(2)(ii)(E) is carried forward subject to section 382(d)(3).

* * * * *

(b) * * *

(4) *Allocation of business interest expense*—(i) *Scope.* This paragraph (b)(4) applies if a loss corporation makes a closing-of-the-books election pursuant to paragraph (b) of this section and has business interest expense in the change year. The rules of this paragraph (b)(4)

apply to determine the amount of deductible current-year business interest expense that is allocable to the pre-change period and the post-change period for purposes of the allocations referred to in paragraph (b)(1) of this section. These rules also apply to determine the amount of any current-year business interest expense that is characterized as disallowed business interest expense allocable to the pre-change period and the post-change period, and to allocate disallowed business interest expense carryforwards to the change year between the pre-change period and the post-change period for deduction.

(ii) *Deductibility of business interest expense.* The rules of this paragraph (b)(4)(ii) apply in the order provided.

(A) The loss corporation calculates its ATI limit, which is the product of its ATI (as defined in § 1.163(j)–1(b)(1)) for the change year and 30 percent. For purposes of this paragraph (b)(4)(ii), the terms *pre-change ATI limit* and *post-change ATI limit* mean the amount of ATI limit allocated to the pre-change period or the post-change period, respectively, computed by allocating an equal portion of the ATI limit to each day in the change year.

(B) Pursuant to paragraph (b)(1) of this section, the loss corporation allocates its current-year business interest expense (including its floor plan financing interest expense) and its business interest income (as defined in § 1.163(j)–1(b)(4)) to the pre-change and post-change periods as if the loss corporation's books were closed on the change date. For purposes of this paragraph (b)(4)(ii), the terms *pre-change BIE* and *post-change BIE* mean the amount of the loss corporation's current-year business interest expense that is allocated to the pre-change period or the post-change period, respectively, under this paragraph (b)(4)(ii)(B).

(C) The loss corporation deducts its pre-change BIE to the extent of its pre-change section 163(j) limit, and the loss corporation deducts its post-change BIE to the extent of its post-change section 163(j) limit. For purposes of this paragraph (b)(4)(ii), the term *pre-change section 163(j) limit* means the sum of the pre-change ATI and the amount of business interest income and floor plan financing interest expense allocated to the pre-change period; the term *post-change section 163(j) limit* means the sum of the post-change ATI limit and the amount of business interest income and floor plan financing interest expense allocated to the post-change period.

(D) If any pre-change BIE or post-change BIE has not been deducted under paragraph (b)(4)(ii)(C) of this section, the loss corporation deducts either any pre-change BIE that has not been deducted to the extent of its surplus post-change section 163(j) limit or any post-change BIE that has not been deducted to the extent of its surplus pre-change section 163(j) limit. For purposes of this paragraph (b)(4)(ii), the term *surplus pre-change section 163(j) limit* means the amount by which the pre-change section 163(j) limit exceeds the amount of pre-change BIE deducted pursuant to paragraph (b)(4)(ii)(C) of this section; the term *surplus post-change section 163(j) limit* means the amount by which the post-change section 163(j) limit exceeds the amount of post-change BIE deducted pursuant to paragraph (b)(4)(ii)(C) of this section.

(E) If the loss corporation has any excess pre-change section 163(j) limit or excess post-change section 163(j) limit, the loss corporation allocates its disallowed business interest expense carryforward, if any, ratably between the pre-change and post-change periods based upon the relative amounts of excess pre-change section 163(j) limit and excess post-change section 163(j) limit. For purposes of this paragraph (b)(4)(ii), the term *excess pre-change section 163(j) limit* means the amount by which the surplus pre-change section 163(j) limit exceeds the amount of post-change BIE deducted pursuant to paragraph (b)(4)(ii)(D) of this section; the term *excess post-change section 163(j) limit* means the amount by which the surplus post-change section 163(j) limit exceeds the amount of pre-change BIE deducted pursuant to paragraph (b)(4)(ii)(D) of this section.

(F) The loss corporation deducts its disallowed business interest expense carryforward that was allocated to the pre-change period under paragraph (b)(4)(ii)(E) of this section to the extent of its excess pre-change section 163(j) limit. Subject to the application of sections 382(b)(3)(B) and 382(d)(3), the loss corporation deducts its disallowed business interest expense carryforward that was allocated to the post-change period under paragraph (b)(4)(ii)(E) of this section to the extent of its excess post-change section 163(j) limit. Any amount of disallowed business interest expense carryforward that is not deducted pursuant to this paragraph (b)(4)(ii)(F) is subject to section 382(d)(3) irrespective of the period to which it was allocated pursuant to paragraph (b)(4)(ii)(E) of this section.

(iii) *Example 1*—(A) *Facts.* X is a calendar-year domestic C corporation that is not a member of a consolidated group. As of January 1, 2021, X has no disallowed business interest expense carryforwards. On October 19, 2021, X experiences an ownership change under section 382(g). For calendar year 2021, X's ATI is $500. For the period beginning on January 1, 2021 and ending on October 19, 2021, X pays or accrues $250 of current-year business interest expense that is deductible but for the potential application of section 163(j), including $50 of floor plan financing interest expense, and X has $60 of business interest income. For the period beginning on October 20, 2021 and ending on December 31, 2021, X pays or accrues $100 of current-year business interest expense that is deductible but for the potential application of section 163(j), including $40 of floor plan financing interest expense, and X has $70 of business interest income. X makes a closing-of-the-books election pursuant to paragraph (b) of this section.

(B) *Analysis*—(*1*) *Calculation and allocation of ATI limit.* For purposes of allocating its net operating loss or taxable income for the change year between the pre-change period and the post-change period under § 1.382–6, X applies paragraph (b)(4) of this section to allocate items related to section 163(j). X's ATI for calendar year 2021 is $500x. Therefore, pursuant to paragraph (b)(4)(ii)(A) of this section, X's ATI limit is $150 ($500 × 30 percent). Additionally, pursuant to paragraph (b)(4)(ii)(A) of this section, X's pre-change ATI limit is $120 ($150 × (292 days/365 days)), and X's post-change ATI limit is $30 ($150 × (73 days/365 days)).

(*2*) *Determination of pre-change BIE and post-change BIE.* Pursuant to paragraph (b)(4)(ii)(B) of this section, X's pre-change BIE and post-change BIE are $250 and $100, respectively.

(*3*) *Determination of pre-change section 163(j) limit and post-change section 163(j) limit.* Pursuant to paragraph (b)(4)(ii)(C) of this section, X's pre-change section 163(j) limit is $230 ($120 (X's pre-change ATI limit) + $60 (X's business interest income allocated to the pre-change period) + $50 (X's floor plan financing interest expense allocated to the pre-change period)). Additionally, pursuant to paragraph (b)(4)(ii)(C) of this section, X's post-change section 163(j) limit is $140 ($30 (X's post-change ATI limit) + $70 (X's business interest income allocated to the post-change period) + $40 (X's floor plan financing interest expense allocated to the post-change period)).

(*4*) *Initial deduction of BIE.* Pursuant to paragraph (b)(4)(ii)(C) of this section, X deducts $230 (its pre-change section 163(j) limit) of its $250 pre-change BIE and all $100 (less than its $140 post-change section 163(j) limit) of its post-change BIE.

(*5*) *Deduction of BIE due to surplus post-change section 163(j) limit.* After applying paragraph (b)(4)(ii)(C) of this section, X has $20 of pre-change BIE that has not been deducted ($250 − $230) and a surplus post-change section 163(j) limit of $40 ($140 − $100). As a result, pursuant to paragraph (b)(4)(ii)(D) of this section, X deducts its remaining $20 of pre-change BIE. (If, after applying paragraph (b)(4)(ii)(C) of this section, X instead had $20 of post-change BIE that had not yet been deducted and a $40 surplus pre-change section 163(j) limit, then X would deduct its remaining $20 of post-change BIE pursuant to paragraph (b)(4)(ii)(D) of this section.)

(iv) *Example 2—Potential deduction of disallowed business interest expense carryforwards.* The facts are the same as in paragraph (b)(4)(iii)(A) of this section, except that, as of January 1, 2021, X has $90 of disallowed business interest expense carryforwards and $150 (rather than $250) of pre-change BIE. X's pre-change section 163(j) limit and post-change section 163(j) limit are the same as in paragraph (b)(4)(iii)(B)(*3*) of this section. Pursuant to paragraph (b)(4)(ii)(C) of this section, X deducts all $150 of its pre-change BIE and all $100 of its post-change BIE. X has no remaining pre-change BIE or post-change BIE to deduct under paragraph (b)(4)(ii)(D) of this section. Paragraph (b)(4)(ii)(E) of this section applies because X has $80 of excess pre-change section 163(j) limit ($230 − $150) and $40 of excess post-change section 163(j) limit ($140 − $100). Under paragraph (b)(4)(ii)(E) of this section, X allocates $60 of its disallowed business interest expense carryforwards to the pre-change period ($90 × ($80/($80 + $40))) and $30 of its disallowed business interest expense carryforwards to the post-change period ($90 × ($40/($80 + $40))). As provided in paragraph (b)(4)(ii)(F) of this section, X deducts all $60 of its disallowed business interest expense carryforwards that are allocated to the pre-change period; subject to the application of section 382, X deducts all $30 of its disallowed business interest expense carryforwards that are allocated to the post-change period.

* * * * *

(h) *Applicability date*—(1) *In general.* This section applies to ownership changes occurring on or after June 22, 1994.

(2) *Ownership changes.* Paragraphs (a) and (b)(1) and (4) of this section apply with respect to an ownership change occurring during a taxable year beginning on or after November 13, 2020. For ownership changes occurring during a taxable year beginning before November 13, 2020, see § 1.382–6 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to testing dates occurring during a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of this section, the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), §§ 1.382–1, 1.382–2, 1.382–5, 1.383–0, and 1.383–1, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, 1.382–7, and 1.383–1), and 1.1504–4, to taxable years beginning after December 31, 2017.

■ **Par. 11.** Section 1.382–7 is amended by adding paragraphs (c), (d), (e), (f), and (g) to read as follows:

§ 1.382–7 Built-in gains and losses.

* * * * *

(c) [Reserved]

(d) *Special rules.* This paragraph (d) contains special rules regarding the identification of recognized built-in losses.

(1)–(4) [Reserved]

(5) *Section 382 disallowed business interest carryforwards.* Section 382 disallowed business interest carryforwards are not treated as recognized built-in losses.

(e)–(f) [Reserved]

(g) *Applicability dates.*

(1)–(3) [Reserved]

(4) Paragraph (d)(5) of this section. Paragraph (d)(5) of this section applies with respect to an ownership change occurring on or after November 13, 2020. For loss corporations that have undergone an ownership change before or after November 13, 2020, see § 1.382–7 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of paragraph (d)(5) of this section to testing dates occurring during a taxable year beginning after December 31, 2017.

■ **Par. 12.** Section 1.383–0 is amended by revising paragraph (a) to read as follows:

§ 1.383–0 Effective date.

(a) The regulations in this part under section 383 of the Code (other than the regulations described in paragraph (b) of this section) reflect the amendments made to sections 382 and 383 by the Tax Reform Act of 1986 and the amendments made to section 382 by Public Law 115–97 (2017). See § 1.383–1(j) for effective date rules.

* * * * *

■ **Par. 13.** Section 1.383–1 is amended by:

■ 1. In paragraph (a):

■ a. Adding entries for paragraphs (d)(1)(i) and (ii);

■ b. Revising the entries for paragraphs (e)(3) and (j);

■ c. Adding entries for paragraphs (j)(1) and (2); and

■ d. Removing the entry for paragraph (k).

■ 2. Removing ''(iv)'' and adding ''(v)'' in its place in paragraph (c)(6)(i)(B).

■ 3. Revising paragraphs (c)(6)(ii) and (d)(1).

■ 4. Removing the commas and adding semicolons in their place at ends of paragraphs (d)(2)(i), (ii), and (vi).

■ 5. Revising paragraph (d)(2)(iii).

■ 6. Redesignating paragraphs (d)(2)(iv) through (vii) as paragraphs (d)(2)(v) through (viii), respectively.

■ 7. Adding a new paragraph (d)(2)(iv).

■ 8. Revising newly redesignated paragraph (d)(2)(v) and paragraph (d)(3)(ii).

■ 9. Removing ''(iv)'' and adding ''(v)'' in its place in paragraph (e)(1).

■ 10. In paragraph (e)(2):

■ a. Removing ''sections 11(b)(2) and (15)'' and adding ''section 15'' in its place in the fourth sentence; and

■ b. Removing the last two sentences.

■ 11. Removing and reserving paragraph (e)(3).

■ 12. In paragraph (f):

■ a. Removing *Example 4;*

■ b. Designating *Examples 1* through *3* as paragraphs (f)(1) through (3), respectively; and

■ c. Revising newly designated paragraphs (f)(2) and (3).

■ 13. In the last sentence of paragraph (g), removing ''(*e.g.,* 0.34 for taxable years beginning in 1989)''.

■ 14. In paragraph (j):

■ a. Revising the subject heading;

■ b. Designating the text of paragraph (j) as paragraph (j)(1) and adding a heading to newly designated paragraph (j)(1); and

■ c. Adding paragraph (j)(2).

■ 15. Removing paragraph (k).

The revisions and additions read as follows:

§ 1.383–1 Special limitations on certain capital losses and excess credits.

(a) * * *

* * * * *

(d) * * *

(1) * * *

(i) In general.

(ii) Ordering rule for losses or credits from same taxable year.

* * * * *

(e) * * *

(3) [Reserved]

* * * * *

(j) Applicability date.

(1) In general.

(2) Interaction with section 163(j).

* * * * *

(c) * * *

(6) * * *

(ii) *Example.* L, a new loss corporation, is a calendar-year taxpayer. L has an ownership change on December 31, 2021. For 2022, L has taxable income (prior to the use of any pre-change losses) of $100,000. In addition, L has a section 382 limitation of $25,000, a pre-change net operating loss carryover of $12,000, a pre-change general business credit carryforward under section 39 of $50,000, and no items described in § 1.383–1(d)(2)(i) through (iv). L's section 383 credit limitation for 2022 is the excess of its regular tax liability computed after allowing a $12,000 net operating loss deduction (taxable income of $88,000; regular tax liability of $18,480), over its regular tax liability computed after allowing an additional deduction in the amount of L's section 382 limitation remaining after the application of paragraphs (d)(2)(i) through (v) of this section, or $13,000 (taxable income of $75,000; regular tax liability of $15,750). L's section 383 credit limitation is therefore $2,730 ($18,480 minus $15,750).

(d) * * *

(1) *In general*—(i) *General rule.* The amount of taxable income of a new loss corporation for any post-change year that may be offset by pre-change losses shall not exceed the amount of the section 382 limitation for the post-change year. The amount of the regular tax liability of a new loss corporation for any post-change year that may be offset by pre-change credits shall not exceed the amount of the section 383 credit limitation for the post-change year.

(ii) *Ordering rule for losses or credits from same taxable year.* A loss corporation's taxable income is offset first by losses subject to a section 382 limitation, to the extent the section 382 limitation for that taxable year has not yet been absorbed, before being offset by losses of the same type from the same taxable year that are not subject to a section 382 limitation. For example, assume that Corporation X has an ownership change in Year 1 and carries over disallowed business interest expense as defined in § 1.163(j)–1(b)(10), some of which constitutes a section 382 disallowed business interest carryforward, from Year 1 to Year 2. To the extent of its section 163(j) limitation, as defined in § 1.163(j)–1(b)(36), and its remaining section 382 limitation, Corporation X offsets its Year 2 income with the section 382 disallowed business interest carryforward before using any of the disallowed business interest expense that is not a section 382 disallowed business interest carryforward. Similar principles apply to the use of tax credits.

(2) * * *

(iii) Pre-change losses that are described in § 1.382–2(a)(2)(iii), other than losses that are pre-change capital losses, that are recognized and are subject to the section 382 limitation in such post-change year;

(iv)(A) With respect to an ownership change date occurring prior to November 13, 2020, but during the taxable year which includes November 13, 2020, the pre-change loss described in section 382(d)(3);

(B) With respect to an ownership change date occurring on or after November 13, 2020, section 382 disallowed business interest carryforwards (within the meaning of § 1.382–2(a)(7));

(v) Pre-change losses not described in paragraphs (d)(2)(i) through (iv) of this section;

* * * * *

(3) * * *

(ii) *Example.* L, a calendar-year taxpayer, has an ownership change on December 31, 2021. For 2022, L has taxable income of $300,000 and a regular tax liability of $63,000. L has no pre-change losses, but it has a business credit carryforward from 2020 of $25,000. L has a section 382 limitation for 2022 of $50,000. L's section 383 credit limitation is $10,500, an amount equal to the excess of L's regular tax liability ($63,000) over its regular tax liability calculated by allowing an additional deduction of $50,000 ($52,500). Pursuant to the limitation contained in section 38(c), however, L is entitled to use only $9,500 (($63,000 − $25,000) × 25 percent) of its business credit carryforward in 2022. The unabsorbed portion of L's section 382 limitation, $1,000 (computed pursuant to paragraph (e) of this section), is carried forward under section 382(b)(2). The unused portion of L's business credit carryforward, $14,500, is carried forward to the extent provided in section 39.

* * * * *

(f) * * *

(2) *Example 2*—(i) *Facts.* L, a calendar-year taxpayer, has an ownership change on December 31, 2021. For 2022, L has $750,000 of ordinary taxable income (before the application of carryovers) and a section 382 limitation of $1,500,000. L's only carryovers are from pre-2021 taxable years and consist of a $500,000 net operating loss (NOL) carryover, and a $200,000 foreign tax credit carryover (all of which may be used under the section 904 limitation). The NOL carryover is a pre-change loss, and the foreign tax credit carryover is a pre-change credit. L has no other pre-change losses or credits that can be used in 2022.

(ii) *Analysis.* The following computation illustrates the application of this section for 2022:

TABLE 1 TO PARAGRAPH (f)(2)(ii)

1. Taxable income before carryovers	$750,000
2. Pre-change NOL carryover	500,000
3. Section 382 limitation	1,500,000
4. Amount of pre-change NOL carryover that can be used (least of line 1, 2, or 3)	500,000
5. Taxable income (line 1 minus line 4)	250,000
6. Section 382 limitation remaining (line 3 minus line 4)	1,000,000
7. Pre-change credit carryover	200,000
8. Regular tax liability (line 5 × section 11 rates)	52,500
9. Modified tax liability (line 5 minus line 6 (but not less than zero) × section 11 rates)	0
10. Section 383 credit limitation (line 8 minus line 9)	52,500
11. Amount of pre-change credits that can be used in 2022 (lesser of line 7 or line 10)	52,500
12. Amount of pre-change credits to be carried over to 2023 under section 904(c) (line 7 minus line 11)	147,500

TABLE 1 TO PARAGRAPH (f)(2)(ii)—Continued

13. Section 383 credit reduction amount: $52,500/0.21	250,000
14. Section 382 limitation to be carried to 2023 under section 382(b)(2) (line 6 minus line 13)	750,000

(3) *Example 3*—(i) *Facts.* L, a calendar-year taxpayer, has an ownership change on December 31, 2021. L has $80,000 of ordinary taxable income (before the application of carryovers) and a section 382 limitation of $25,000 for 2022, a post-change year. L's only carryover is from a pre-2021 taxable year and is a general business credit carryforward under section 39 in the amount of $10,000 (no portion of which is attributable to the investment tax credit under section 46). The general business credit carryforward is a pre-change credit. L has no other credits which can be used in 2022.

(ii) *Analysis.* The following computation illustrates the application of this section:

TABLE 2 TO PARAGRAPH (f)(3)(ii)

1. Taxable income before carryovers	$80,000
2. Section 382 limitation	25,000
3. Pre-change credit carryover	10,000
4. Regular tax liability (line 1 × section 11 rates)	16,800
5. Modified tax liability ((line 1 minus line 2) × section 11 rates)	11,550
6. Section 383 credit limitation (line 4 minus line 5)	5,250
7. Amount of pre-change credits that can be used (lesser of line 3 or line 6)	5,250
8. Amount of pre-change credits to be carried over to 2023 under sections 39 and 382(l)(2) (line 3 minus line 7)	4,750
9. Regular tax payable (line 4 minus line 7)	11,550
10. Section 383 credit reduction amount: $5,250/0.21	25,000
11. Section 382 limitation to be carried to 2023 under section 382(b)(2) (line 2 minus line 10)	0

* * * * *

(j) Applicability date—(1) *In general.* * * *

(2) *Interaction with section 163(j).* Paragraphs (c)(6)(i)(B) and (c)(6)(ii), (d)(1), (d)(2)(iii) through (viii), (d)(3)(ii), (e)(1) through (3), (f), and (g) of this section apply with respect to ownership changes occurring during a taxable year beginning on or after November 13, 2020. For loss corporations that have undergone an ownership change during a taxable year beginning before November 13, 2020, see § 1.383–1 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to an ownership change occurring during a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply either the rules of this section (except paragraph (d)(2)(iv)(B) of this section), the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), §§ 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, and 1.383–0, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, § 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4; or the rules of this section (except paragraph (d)(2)(iv)(A) of this section), the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)) and §§ 1.382–1, 1.382–2, 1.382–5, 1.382–6, and 1.383–0, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, 1.382–7, and 1.383–1), and 1.1504–4, to those ownership changes.

■ **Par. 14.** Section 1.446–3 is amended by revising paragraphs (g)(4) and (j)(2) to read as follows:

§ 1.446–3 Notional principal contracts.

* * * * *

(g) * * *

(4) *Swaps with significant nonperiodic payments*—(i) *General rule.* Except as provided in paragraph (g)(4)(ii) of this section, a swap with significant nonperiodic payments is treated as two separate transactions consisting of an on-market, level payment swap and a loan. The loan must be accounted for by the parties to the contract independently of the swap. The time value component associated with the loan, determined in accordance with paragraph (f)(2)(iii)(A) of this section, is recognized as interest expense to the payor and interest income to the recipient.

(ii) *Exception for cleared swaps and non-cleared swaps subject to margin or collateral requirements.* Paragraph (g)(4)(i) of this section does not apply to a swap if the contract is described in paragraph (g)(4)(ii)(A) or (B) of this section.

(A) The swap is cleared by a derivatives clearing organization, as such term is defined in section 1a of the Commodity Exchange Act (7 U.S.C. 1a), or by a clearing agency, as such term is defined in section 3 of the Securities Exchange Act of 1934 (15 U.S.C. 78c), that is registered as a derivatives clearing organization under the Commodity Exchange Act or as a clearing agency under the Securities Exchange Act of 1934, respectively, and the derivatives clearing organization or clearing agency requires the parties to the swap to post and collect margin or collateral.

(B) The swap is a non-cleared swap that requires the parties to meet the margin or collateral requirements of a federal regulator or that provides for margin or collateral requirements that are substantially similar to a cleared swap or a non-cleared swap subject to the margin or collateral requirements of a federal regulator. For purposes of this paragraph (g)(4)(ii)(B), the term *federal regulator* means the Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), or a prudential regulator, as defined in section 1a(39) of the Commodity Exchange Act (7 U.S.C. 1a), as amended by section 721 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Public Law 111–203, 124 Stat. 1376, Title VII.

(iii) *Coordination with section 163(j).* For the treatment of swaps with significant nonperiodic payments under section 163(j), see § 1.163(j)–1(b)(22)(ii).

* * * * *

(j) * * *

(2) The rules provided in paragraph (g)(4) of this section apply to notional principal contracts entered into on or after September 14, 2021. Taxpayers may choose to apply the rules provided in paragraph (g)(4) of this section to notional principal contracts entered into before September 14, 2021.

■ **Par. 15.** Section 1.469–9 is amended by revising paragraph (b)(2) to read as follows:

§ 1.469–9 Rules for certain rental real estate activities.

* * * * *

(b) * * *

(2) *Real property trade or business.* The following terms have the following meanings in determining whether a trade or business is a real property trade or business for purposes of section 469(c)(7)(C) and this section.

(i) *Real property*—(A) *In general.* The term *real property* includes land, buildings, and other inherently permanent structures that are permanently affixed to land. Any interest in real property, including fee ownership, co-ownership, a leasehold, an option, or a similar interest is real property under this section. Tenant improvements to land, buildings, or other structures that are inherently permanent or otherwise classified as real property under this section are real property for purposes of section 469(c)(7)(C). However, property manufactured or produced for sale that is not real property in the hands of the manufacturer or producer, but that may be incorporated into real property through installation or any similar process or technique by any person after the manufacture or production of such property (for example, bricks, nails, paint, and windowpanes), is not treated as real property in the hands of any person (including any person involved in the manufacture, production, sale, incorporation or installation of such property) prior to the completed incorporation or installation of such property into the real property for purposes of section 469(c)(7)(C) and this section.

(B) *Land.* The term *land* includes water and air space superjacent to land and natural products and deposits that are unsevered from the land. Natural products and deposits, such as plants, crops, trees, water, ores, and minerals, cease to be real property when they are harvested, severed, extracted, or removed from the land. Accordingly, any trade or business that involves the cultivation and harvesting of plants, crops, or certain types of trees in a farming operation as defined in section 464(e), or severing, extracting, or removing natural products or deposits from land is not a real property trade or business for purposes of section 469(c)(7)(C) and this section. The storage or maintenance of severed or extracted natural products or deposits, such as plants, crops, trees, water, ores, and minerals, in or upon real property does not cause the stored property to be recharacterized as real property, and any trade or business relating to or involving such storage or maintenance of severed or extracted natural products or deposits is not a real property trade or business, even though such storage or maintenance otherwise may occur upon or within real property.

(C) *Inherently permanent structure.* The term *inherently permanent structure* means any permanently affixed building or other permanently affixed structure. If the affixation is reasonably expected to last indefinitely, based on all the facts and circumstances, the affixation is considered permanent. However, an asset that serves an active function, such as an item of machinery or equipment (for example, HVAC system, elevator or escalator), is not a building or other inherently permanent structure, and therefore is not real property for purposes of section 469(c)(7)(C) and this section, even if such item of machinery or equipment is permanently affixed to or becomes incorporated within a building or other inherently permanent structure. Accordingly, a trade or business that involves the manufacture, installation, operation, maintenance, or repair of any asset that serves an active function will not be a real property trade or business, or a unit or component of another real property trade or business, for purposes of section 469(c)(7)(C) and this section.

(D) *Building*—(*1*) *In general.* A *building* encloses a space within its walls and is generally covered by a roof or other external upper covering that protects the walls and inner space from the elements.

(*2*) *Types of buildings.* Buildings include the following assets if permanently affixed to land: Houses; townhouses; apartments; condominiums; hotels; motels; stadiums; arenas; shopping malls; factory and office buildings; warehouses; barns; enclosed garages; enclosed transportation stations and terminals; and stores.

(E) *Other inherently permanent structures*—(*1*) *In general.* Other inherently permanent structures include the following assets if permanently affixed to land: Parking facilities; bridges; tunnels; roadbeds; railroad tracks; pipelines; storage structures such as silos and oil and gas storage tanks; and stationary wharves and docks.

(*2*) *Facts and circumstances determination.* The determination of whether an asset is an inherently permanent structure is based on all the facts and circumstances. In particular, the following factors must be taken into account:

(*i*) The manner in which the asset is affixed to land and whether such manner of affixation allows the asset to be easily removed from the land;

(*ii*) Whether the asset is designed to be removed or to remain in place indefinitely on the land;

(*iii*) The damage that removal of the asset would cause to the asset itself or to the land to which it is affixed;

(*iv*) Any circumstances that suggest the expected period of affixation is not indefinite (for example, a lease that requires or permits removal of the asset from the land upon the expiration of the lease); and

(*v*) The time and expense required to move the asset from the land.

(ii) *Other definitions*—(A) through (G) [Reserved]

(H) *Real property operation.* The term *real property operation* means handling, by a direct or indirect owner of the real property, the day-to-day operations of a trade or business, under paragraph (b)(1) of this section, relating to the maintenance and occupancy of the real property that affect the availability and functionality of that real property used, or held out for use, by customers where payments received from customers are principally for the customers' use of the real property. The principal purpose of such business operations must be the provision of the use of the real property, or physical space accorded by or within the real property, to one or more customers, and not the provision of other significant or extraordinary personal services, under § 1.469–1T(e)(3)(iv) and (v), to customers in conjunction with the customers' incidental use of the real property or physical space. If the real property or physical space is provided to a customer to be used to carry on the customer's trade or business, the principal purpose of the business operations must be to provide the customer with exclusive use of the real property or physical space in furtherance of the customer's trade or business, and not to provide other significant or extraordinary personal services to the customer in addition to or in conjunction with the use of the real property or physical space, regardless of whether the customer pays for the services separately. However, for purposes of and with respect to the preceding sentence, other incidental personal services may be provided to the customer in conjunction with the use of real property or physical space, as long as such services are insubstantial in relation to the customer's use of the real property or physical space.

(I) *Real property management.* The term *real property management* means handling, by a professional manager, the day-to-day operations of a trade or business, under paragraph (b)(1) of this section, relating to the maintenance and occupancy of real property that affect the availability and functionality of that property used, or held out for use, by customers where payments received from customers are principally for the customers' use of the real property. The principal purpose of such business operations must be the provision of the use of the real property, or physical space accorded by or within the real property, to one or more customers, and not the provision of other significant or extraordinary personal services, under § 1.469–1T(e)(3)(iv) and (v), to customers in conjunction with the customers' incidental use of the real property or physical space. If the real property or physical space is provided to a customer to be used to carry on the customer's trade or business, the principal purpose of the business operations must be to provide the customer with exclusive use of the real property or physical space in furtherance of the customer's trade or business, and not to provide other significant or extraordinary personal services to the customer in addition to or in conjunction with the use of the real property or physical space, regardless of whether the customer pays for the services separately. However, for purposes of and with respect to the preceding sentence, other incidental personal services may be provided to the customer in conjunction with the use of real property or physical space, as long as such services are insubstantial in relation to the customer's use of the real property or physical space. A professional manager is a person responsible, on a full-time basis, for the overall management and oversight of the real property or properties and who is not a direct or indirect owner of the real property or properties.

(iii) *Examples.* The following examples illustrate the operation of this paragraph (b)(2):

(A) *Example 1.* A owns farmland and uses the land in A's farming business to grow and harvest crops of various kinds. As part of this farming business, A utilizes a greenhouse that is an inherently permanent structure to grow certain crops during the winter months. Under the rules of this section, any trade or business that involves the cultivation and harvesting of plants, crops, or trees is not a real property trade or business for purposes of section 469(c)(7)(C) and this section, even though the cultivation and harvesting of crops occurs upon or within real property. Accordingly, under these facts, A is not engaged in a real property trade or business for purposes of section 469(c)(7)(C) and this section.

(B) *Example 2.* B is a retired farmer and owns farmland that B rents exclusively to C to operate a farm. The arrangement between B and C is a trade or business (under paragraph (b)(1) of this section) where payments by C are principally for C's use of B's real property. B also provides certain farm equipment for C's use. However, C is solely responsible for the maintenance and repair of the farm equipment along with any costs associated with operating the equipment. B also occasionally provides oral advice to C regarding various aspects of the farm operation, based on B's prior experience as a farmer. Other than the provision of this occasional advice, B does not provide any significant or extraordinary personal services to C in connection with the rental of the farmland to C. Under these facts, B is engaged in a real property trade or business (which does not include the use or deemed rental of any farm equipment) for purposes of section 469(c)(7)(C) and this section, and B's oral advice is an incidental personal service that B provides in conjunction with C's use of the real property. Nevertheless, under these facts, C is not engaged in a real property trade or business for purposes of section 469(c)(7)(C) and this section because C is engaged in the business of farming.

(C) *Example 3.* D owns a building in which D operates a restaurant and bar. Even though D provides customers with use of the physical space inside the building, D is not engaged in a trade or business where payments by customers are principally for the use of real property or physical space. Instead, the payments by D's customers are principally for the receipt of significant or extraordinary personal services (under § 1.469–1T(e)(3)(iv) and (v)), mainly food and beverage preparation and presentation services, and the use of the physical space by customers is incidental to the receipt of these personal services. Under the rules of this section, any trade or business that involves the provision of significant or extraordinary personal services to customers in conjunction with the customers' incidental use of real property or physical space is not a real property trade or business, even though the business operations occur upon or within real property. Accordingly, under these facts, D is not engaged in a real property trade or business for purposes of section 469(c)(7)(C) and this section.

(D) *Example 4.* E owns a majority interest in an S corporation, X, that is engaged in the trade or business of manufacturing industrial cooling systems for installation in commercial buildings and for other uses. E also owns a majority interest in an S corporation, Y, that purchases the industrial cooling systems from X and that installs, maintains, and repairs those systems in both existing commercial buildings and commercial buildings under construction. Under the rules of this section, any trade or business that involves the manufacture, installation, operation, maintenance, or repair of any machinery or equipment that serves an active function will not be a real property trade or business (or a unit or component of another real property trade or business) for purposes of section 469(c)(7)(C) and this section, even though the machinery or equipment will be permanently affixed to real property once it is installed. In this case, the industrial cooling systems are machinery or equipment that serves an active function. Accordingly, under these facts, E, X and Y will not be treated as engaged in one or more real property trades or businesses for purposes of section 469(c)(7)(C) and this section.

(E) *Example 5.* (*1*) F owns an interest in P, a limited partnership. P owns and operates a luxury hotel. In addition to providing rooms and suites for use by customers, the hotel offers many additional amenities such as in-room food and beverage service, maid and linen service, parking valet service, concierge service, front desk and bellhop service, dry cleaning and laundry service, and in-room barber and hairdresser service. P contracted with M to provide maid and janitorial services to P's hotel. M is an S corporation principally engaged in the trade or business of providing maid and janitorial services to various types of businesses, including hotels. G is a professional manager employed by M who handles the day-to-day business operations relating to M's provision of maid and janitorial services to M's various customers, including P.

(*2*) Even though the personal services that P provides to the customers of its hotel are significant personal services under § 1.469–1T(e)(3)(iv), the principal purpose of P's hotel business operations is the provision of use of the hotel's rooms and suites to customers, and not the provision of the significant personal services to P's customers in conjunction with the customers' incidental use of those rooms or suites. The provision of these significant personal services by P to P's customers is incidental to the customers' use of the hotel's real property. Accordingly, under these facts, F is treated as owning an interest in a real property trade or business conducted by or through P and P is treated as engaged in a real property trade or business for purposes of section 469(c)(7)(C) and this section.

(*3*) With respect to the maid and janitorial services provided by M, M's operations affect the availability and functionality of real property used, or held out for use, by customers in a trade or business where payments by customers are principally for the use of real property (in this case, P's hotel). However, M does not operate or manage real property. Instead, M is engaged in a trade or business of providing maid and janitorial services to customers, such as P, that are engaged in real property trades or businesses. Thus, M's business operations are merely ancillary to real property trades or businesses. Therefore, M is not engaged in real property operations or management as defined in this section. Accordingly, under these facts, M is not engaged in a real property trade or business under section 469(c)(7)(C) and this section.

(*4*) With respect to the day-to-day business operations that G handles as a professional manager of M, the business operations that G manages is not the provision of use of P's hotel rooms and suites to customers. G does not operate or manage real property. Instead, G manages the provision of maid and janitorial services to customers, including P's hotel. Therefore, G is not engaged in real property management as defined in this section. Accordingly, under these facts, G is not engaged in a real property trade or business under section 469(c)(7)(C) and this section.

* * * * *

■ **Par. 16.** Section 1.469–11 is amended by:

■ 1. Revising the section heading;

■ 2. Removing the period at the end of paragraph (a)(1) and adding a semicolon in its place;

■ 3. Revising paragraph (a)(3);

■ 4. Redesignating paragraphs (a)(4) and (5) as paragraphs (a)(5) and (6), respectively; and

■ 5. Adding a new paragraph (a)(4).

The revision and addition read as follows:

§ 1.469–11 Applicability date and transition rules.

(a) * * *

(3) The rules contained in § 1.469–9, other than paragraph (b)(2), apply for taxable years beginning on or after January 1, 1995, and to elections made under § 1.469–9(g) with returns filed on or after January 1, 1995;

(4) The rules contained in § 1.469–9(b)(2) apply to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, under sections 267(b) and 707(b)(1), may choose to apply the rules of § 1.469–9(b)(2) for a taxable year beginning after December 31, 2017, so long as they consistently apply the rules of § 1.469–9(b)(2), the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, 1.382–7, and 1.383–1), and 1.1504–4 to that taxable year;

* * * * *

■ **Par. 17.** Section 1.704–1 is amended by adding paragraph (b)(4)(xi) to read as follows:

§ 1.704–1 Partner's distributive share.

* * * * *

(b) * * *

(4) * * *

(xi) *Section 163(j) excess items.* Allocations of section 163(j) excess items as defined in § 1.163(j)–6(b)(6) do not have substantial economic effect under paragraph (b)(2) of this section and, accordingly, such expenditures must be allocated in accordance with the partners' interests in the partnership. See paragraph (b)(3)(iv) of this section. Allocations of section 163(j) excess items will be deemed to be in accordance with the partners' interests in the partnership if such allocations are made in accordance with § 1.163(j)–6(f).

* * * * *

■ **Par. 18.** Section 1.860C–2 is amended by revising paragraph (b)(2) to read as follows:

§ 1.860C–2 Determination of REMIC taxable income or net loss.

* * * * *

(b) * * *

(2) *Deduction allowable under section 163*—(i) A REMIC is allowed a deduction, determined without regard to section 163(d), for any interest expense accrued during the taxable year.

(ii) For taxable years beginning after December 31, 2017, a REMIC is allowed a deduction, determined without regard to section 163(j), for any interest expense accrued during the taxable year.

* * * * *

■ **Par. 19.** Section 1.1362–3 is amended by:

■ 1. Redesignating the text in paragraph (c)(3) as paragraph (c)(3)(i), adding a subject heading to newly redesignated paragraph (c)(3)(i), and adding paragraph (c)(3)(ii); and

■ 2. Designating *Examples 1* through *4* of paragraph (d) as paragraphs (d)(1) through (d)(4), respectively.

The additions read as follows:

§ 1.1362–3 Treatment of S termination year.

* * * * *

(c) * * *

(3) * * *

(i) *In general.* * * *

(ii) *Application of section 163(j).* For purposes of section 163(j), a separate limitation (as defined in § 1.163(j)–1(b)(36)) applies to each S short year and each C short year. Any items necessary to determine the amount of business interest expense (as defined in § 1.163(j)–1(b)(3)) that are deducted in each S short year or C short year must be allocated between the S short year and C short year in accordance with an allocation methodology provided in section 1362(e).

* * * * *

■ **Par. 20.** Section 1.1368–1 is amended by adding a sentence to the end of paragraph (g)(2)(ii) to read as follows:

§ 1.1368–1 Distributions by S corporations.

* * * * *

(g) * * *

(2) * * *

(ii) * * * In the case of a taxable year for which an election is made under paragraph (g)(2)(i), for purposes of section 163(j), a separate section 163(j) limitation (as defined in § 1.163(j)–1(b)(36)) applies to each separate taxable year. Any items necessary to determine the amount of business interest expense (as defined in § 1.163(j)–1(b)(3)) that are deducted in each separate taxable year must be allocated between the two separate taxable years in accordance with an allocation methodology provided in this paragraph (g).

* * * * *

■ **Par. 21.** Section 1.1377–1 is amended by:

■ 1. Redesignating paragraphs (b)(3)(ii) through (iv) as paragraphs (b)(3)(iii) through (v), respectively; and

■ 2. Adding a new paragraph (b)(3)(ii).

The addition reads as follows:

§ 1.1377–1 Pro rata share.

* * * * *

(b) * * *

(3) * * *

(ii) *Section 163(j).* If a terminating election is made to treat the S corporation's taxable year as consisting of separate taxable years, for purposes of section 163(j), a separate limitation (as defined in § 1.163(j)–1(b)(36)) will apply to each separate taxable year. Any items necessary to determine the amount of business interest expense (as defined in § 1.163(j)–1(b)(3)) that are deducted in each separate taxable year must be allocated between the separate taxable years in accordance with an allocation methodology provided in this section.

* * * * *

■ **Par. 22.** Section 1.1502–13 is amended:

■ 1. In paragraph (a)(6)(ii), under the heading ''Anti-avoidance rules. (§ 1.1502–13(h)(2))'', by:

■ i. Designating *Examples 1* through *5* as entries (i) through (v); and

■ ii. Adding an entry (vi);

■ 2. In paragraph (h)(2) by:

■ a. Designating *Examples 1* through *5* as paragraphs (h)(2)(i) through (v), respectively.

■ b. In newly designated paragraphs (h)(2)(i) through (v):

■ i. Redesignating paragraphs (h)(2)(i)(a) and (b) as paragraphs (h)(2)(i)(A) and (B);

■ ii. Redesignating paragraphs (h)(2)(ii)(a) and (b) as paragraphs (h)(2)(ii)(A) and (B);

■ iii. Redesignating paragraphs (h)(2)(iii)(a) and (b) as paragraphs (h)(2)(iii)(A) and (B);

■ iv. Redesignating paragraphs (h)(2)(iv)(a) and (b) as paragraphs (h)(2)(iv)(A) and (B);

■ v. Redesignating paragraphs (h)(2)(v)(a) and (b) as paragraphs (h)(2)(iv)(A) and (B); and

■ c. Adding paragraph (h)(2)(vi).

The additions read as follows:

§ 1.1502–13 Intercompany transactions.

(a) * * *

(6) * * *

(ii) * * *

Anti-avoidance rules. (§ 1.1502–13(h)(2))

* * * * *

(vi) *Example 6.* Section 163(j) interest limitation.

* * * * *

(h) * * *

(2) * * *

(vi) *Example 6: Section 163(j) interest limitation*—(A) *Facts.* S1 and S2 are members of a consolidated group of which P is the common parent. S1 is engaged in an excepted trade or business, and S2 is engaged in a non-excepted trade or business. If S1 were to lend funds directly to S2 in an intercompany transaction, under § 1.163(j)–10(a)(4)(i), the intercompany obligation of S2 would not be considered an asset of S1 for purposes of § 1.163(j)–10 (concerning allocations of interest and other taxable items between excepted and non-excepted trades or businesses for purposes of section 163(j)). With a principal purpose of avoiding treatment of a lending transaction between S1 and S2 as an intercompany transaction (and increasing the P group's basis in its assets allocable to excepted trades or businesses), S1 lends funds to X (an unrelated third party). X then on-lends funds to S2 on substantially similar terms.

(B) *Analysis.* A principal purpose of the steps undertaken was to avoid treatment of a lending transaction between S1 and S2 as an intercompany transaction. Therefore, under paragraph (h)(1) of this section, appropriate adjustments are made, and the X obligation in the hands of S1 is not treated as an asset of S1 for purposes of § 1.163(j)–10, to the extent of the loan from X to S2.

* * * * *

■ **Par. 23.** Section 1.1502–21 is amended by adding new paragraph (c)(3) to read as follows:

§ 1.1502–21 Net operating losses.

* * * * *

(c) * * *

(3) *Cross-reference.* For rules governing the application of a SRLY limitation to business interest expense for which a deduction is disallowed under section 163(j), see § 1.163(j)–5(d) and (f).

* * * * *

■ **Par. 24.** Section 1.1502–36 is amended by:

■ 1. Revising the second sentence of paragraph (f)(2);

■ 2. Revising the paragraph (h) heading;

■ 3. Designating the text of paragraph (h) as paragraph (h)(1) and adding a heading to newly designated paragraph (h)(1); and

■ 4. Adding paragraph (h)(2).

The revisions and addition read as follows:

§ 1.1502–36 Unified loss rule.

* * * * *

(f) * * *

(2) * * * Such provisions include, for example, sections 163(j), 267(f), and 469, and § 1.1502–13. * * *

* * * * *

(h) *Applicability date*—(1) *In general.* * * *

(2) *Definition in paragraph (f)(2) of this section.* Paragraph (f)(2) of this section applies to taxable years beginning on or after November 13, 2020. For taxable years beginning before November 13, 2020, see § 1.1502–36 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, and before November 13, 2020, so long as the taxpayers and their related parties consistently apply the rules of this section, the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, 1.382–7, and 1.383–1), and 1.1504–4, to that taxable year.

■ **Par. 25.** Section 1.1502–79 is amended by adding paragraph (f) to read as follows:

§ 1.1502–79 Separate return years.

* * * * *

(f) *Disallowed business interest expense carryforwards.* For the treatment of disallowed business interest expense carryforwards (as defined in § 1.163(j)–1(b)(11)) of a member arising in a separate return limitation year, see § 1.163(j)–5(d) and (f).

■ **Par. 26.** Section 1.1502–90 is amended by revising the entry for § 1.1502–98 and adding an entry for § 1.1502–99(d) to read as follows:

§ 1.1502–90 Table of contents.

* * * * *

§ 1.1502–98 Coordination with sections 383 and 163(j).

§ 1.1502–99 Effective dates.

* * * * *

(d) Application to section 163(j).

■ **Par. 27.** Section 1.1502–91 is amended by revising paragraph (e)(2) to read as follows:

§ 1.1502–91 Application of section 382 with respect to a consolidated group.

* * * * *

(e) * * *

(2) *Example*—(i) *Facts.* The L group has a consolidated net operating loss arising in Year 1 that is carried over to Year 2. The L loss group has an ownership change at the beginning of Year 2.

(ii) *Analysis.* The net operating loss carryover of the L loss group from Year 1 is a pre-change consolidated attribute because the L group was entitled to use the loss in Year 2 and therefore the loss was described in paragraph (c)(1)(i) of this section. Under paragraph (a)(2)(i) of this section, the amount of consolidated taxable income of the L group for Year 2 that may be offset by this loss carryover may not exceed the consolidated section 382 limitation of the L group for that year. See § 1.1502–93 for rules relating to the computation of the consolidated section 382 limitation.

(iii) *Business interest expense.* The facts are the same as in the *Example* in paragraph (e)(2)(i) of this section, except that, rather than a consolidated net operating loss, a member of the L group pays or accrues a business interest expense in Year 1 for which a deduction is disallowed in that year under section 163(j) and § 1.163(j)–2(b). The disallowed business interest expense is carried over to Year 2 under section 163(j)(2) and § 1.163(j)–2(c). Thus, the disallowed business interest expense carryforward is a pre-change loss. Under section 163(j), the L loss group is entitled to deduct the carryforward in Year 2; however, the amount of consolidated taxable income of the L group for Year 2 that may be offset by this carryforward may not exceed the consolidated section 382 limitation of the L group for that year. See § 1.1502–98(b) (providing that §§ 1.1502–91 through 1.1502–96 apply section 382 to business interest expense, with appropriate adjustments).

* * * * *

■ **Par. 28.** Section 1.1502–95 is amended in paragraph (b)(4) by:

■ 1. Designating *Examples 1* and *2* as paragraphs (b)(4)(i) and (ii), respectively;

■ 2. In newly designated paragraph (b)(4)(i), redesignating paragraphs (b)(4)(i)(i) and (ii) as paragraphs (b)(4)(i)(A) and (B), respectively;

■ 3. In newly designated paragraph (b)(4)(ii), redesignating paragraphs (b)(4)(ii)(i) and (ii) as paragraphs (b)(4)(ii)(A) and (B), respectively; and

■ 4. Adding two sentences at the end of newly redesignated paragraph (b)(4)(ii)(B).

The additions read follows:

§ 1.1502–95 Rules on ceasing to be a member of a consolidated group (or loss subgroup).

* * * * *

(b) * * *

(4) * * *

(ii) * * *

(B) * * * The analysis would be similar if the L loss group had an ownership change under § 1.1502–92 in Year 2 with respect to disallowed business interest expense paid or accrued by L2 in Year 1 and carried forward under section 163(j)(2) to Year 2 and Year 3. See § 1.1502–98(b) (providing that §§ 1.1502–91 through 1.1502–96 apply section 382 to business interest expense, with appropriate adjustments).

* * * * *

■ **Par. 29.** Section 1.1502–98 is amended by:

■ 1. Revising the section heading;

■ 2. Designating the undesignated text as paragraph (a) and adding a subject heading for newly designated paragraph (a); and

■ 3. Adding paragraph (b).

The revision and additions read as follows:

§ 1.1502–98 Coordination with sections 383 and 163(j).

(a) *Coordination with section 383.* * * *

(b) *Application to section 163(j)*—(1) *In general.* The regulations in this part under sections 163(j), 382, and 383 of the Code contain rules governing the application of section 382 to interest expense governed by section 163(j) and the regulations in this part under section 163(j) of the Code. See, for example, §§ 1.163(j)–11(c), 1.382–2, 1.382–6, 1.382–7, and 1.383–1. The rules contained in §§ 1.1502–91 through 1.1502–96 apply these rules to members of a consolidated group, or corporations that join or leave a consolidated group, with appropriate adjustments. For example, for purposes of §§ 1.1502–91 through 1.1502–96, the term *loss group* includes a consolidated group in which any member is entitled to use a disallowed business interest expense carryforward, as defined in § 1.163(j)–1(b)(11), that did not arise, and is not treated as arising, in a SRLY with regard to that group. Additionally, a reference to net operating loss carryovers in §§ 1.1502–91 through 1.1502–96 generally includes a reference to disallowed business interest expense carryforwards. References to a loss or losses in §§ 1.1502–91 through 1.1502–96 include references to disallowed business interest expense carryforwards or section 382 disallowed business interest carryforwards, within the meaning of § 1.382–2(a)(7), as appropriate.

(2) *Appropriate adjustments.* For purposes of applying the rules in §§ 1.1502–91 through 1.1502–96 to current-year business interest expense (as defined in § 1.163(j)–1(b)(9)), disallowed business interest expense carryforwards, and section 382 disallowed business interest carryforwards, appropriate adjustments are required.

■ **Par. 30.** Section 1.1502–99 is amended by adding paragraph (d) to read as follows:

§ 1.1502–99 Effective/applicability dates.

* * * * *

(d) *Application to section 163(j)*—(1) *Sections 1.382–2 and 1.382–5.* To the extent the rules of §§ 1.1502–91 through 1.1502–99 effectuate the rules of §§ 1.382–2 and 1.382–5, the provisions apply with respect to ownership changes occurring on or after November 13, 2020. For loss corporations that have ownership changes occurring before November 13, 2020, see §§ 1.1502–91 through 1.1502–99 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of §§ 1.1502–91 through 1.1502–99 to the extent they apply the rules of §§ 1.382–2 and 1.382–5, to ownership changes occurring during a taxable year beginning after December 31, 2017, as well as consistently applying the rules of the §§ 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–6 and 1.383–1), the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–7, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–79, and 1.1504–4, to that taxable year.

(2) *Sections 1.382–6 and 1.383–1.* To the extent the rules of §§ 1.1502–91 through 1.1502–98 effectuate the rules of §§ 1.382–6 and 1.383–1, the provisions apply with respect to ownership changes occurring during a taxable year beginning on or after November 13, 2020. For the application of these rules to an ownership change with respect to an ownership change

occurring during a taxable year beginning before November 13, 2020, see §§ 1.1502–91 through 1.1502–99 as contained in 26 CFR part 1, revised April 1, 2019. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of §§ 1.1502–91 through 1.1502–99 (to the extent that those rules effectuate the rules of §§ 1.382–6 and 1.383–1), to ownership changes occurring during a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of 1.1502–91 through 1.1502–99 (to the extent that those rules effectuate the rules of §§ 1.382–2 and 1.382–5), the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–7, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, and 1.1504–4, to a taxable year beginning after December 31, 2017.

■ **Par. 31.** Section 1.1504–4 is amended by:

■ 1. Removing ''163(j), 864(e),'' from the first sentence of paragraph (a)(2) and adding ''864(e)'' in its place; and

■ 2. Adding two sentences at the end of paragraph (i).

The additions read as follows:

§ 1.1504–4 Treatment of warrants, options, convertible obligations, and other similar interests.

* * * * *

(i) * * * Paragraph (a)(2) of this section applies with respect to taxable years beginning on or after November 13, 2020. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of this section, the section 163(j) regulations (as defined in § 1.163(j)–1(b)(37)), and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, 1.382–7, and 1.383–1), to that taxable year.

Sunita Lough,

Deputy Commissioner for Services and Enforcement.

Approved: July 14, 2020.

David J. Kautter,

Assistant Secretary of the Treasury (Tax Policy).

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG–107911–18]

RIN 1545–BP73

Limitation on Deduction for Business Interest Expense; Allocation of Interest Expense by Passthrough Entities; Dividends Paid by Regulated Investment Companies; Application of Limitation on Deduction for Business Interest Expense to United States Shareholders of Controlled Foreign Corporations and to Foreign Persons With Effectively Connected Income

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This notice of proposed rulemaking provides rules concerning the limitation on the deduction for business interest expense after amendment of the Internal Revenue Code (Code) by the provisions commonly known as the Tax Cuts and Jobs Act, which was enacted on December 22, 2017, and the Coronavirus Aid, Relief, and Economic Security Act, which was enacted on March 27, 2020. Specifically, these proposed regulations address application of the limitation in contexts involving passthrough entities, regulated investment companies (RICs), United States shareholders of controlled foreign corporations, and foreign persons with effectively connected income in the United States. These proposed regulations also provide guidance regarding the definitions of real property development, real property redevelopment, and a syndicate. These proposed regulations affect taxpayers that have business interest expense, particularly passthrough entities, their partners and shareholders, as well as foreign corporations and their United States shareholders and foreign persons with effectively connected income. These proposed regulations also affect RICs that have business interest income, RIC shareholders that have business interest expense, and members of a consolidated group.

DATES: Written or electronic comments and requests for a public hearing must be received by November 2, 2020, which is 60 days after the date of filing for public inspection with the Office of the Federal Register.

ADDRESSES: Commenters are strongly encouraged to submit public comments electronically. Submit electronic submissions via the Federal eRulemaking Portal at *www.regulations.gov* (indicate IRS and REG–107911–18) by following the online instructions for submitting comments. Once submitted to the Federal eRulemaking Portal, comments cannot be edited or withdrawn. The IRS expects to have limited personnel available to process public comments that are submitted on paper through mail. The Department of the Treasury (Treasury Department) and the IRS will publish for public availability any comment submitted electronically, and when practicable on paper, to its public docket.

Send paper submissions to: CC:PA:LPD:PR (REG–107911–18), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

FOR FURTHER INFORMATION CONTACT: Concerning § 1.163(j)–1, Steven Harrison, (202) 317–6842, Michael Chin, (202) 317–6842 or John Lovelace, (202) 317–5363; concerning § 1.163(j)–2, Sophia Wang, (202) 317–4890 or John Lovelace, (202) 317–5363, concerning § 1.163–14, § 1.163(j)–6, or § 1.469–9, William Kostak, (202) 317–5279 or Anthony McQuillen, (202) 317–5027; concerning § 1.163–15, Sophia Wang, (202) 317–4890; concerning § 1.163(j)–7 or § 1.163(j)–8, Azeka J. Abramoff, (202) 317–3800 or Raphael J. Cohen, (202) 317–6938, concerning § 1.1256(e)–2, Sophia Wang, (202) 317–4890 or Pamela Lew, (202) 317–7053; concerning submissions of comments and/or requests for a public hearing, Regina L. Johnson, (202) 317–5177 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Income Tax Regulations (26 CFR part 1) under sections 163 (in particular section 163(j)), 469 and 1256(e) of the Code. Section 163(j) was amended as part of Public Law 115–97, 131 Stat. 2054 (December 22, 2017), commonly referred to as the Tax Cuts and Jobs Act (TCJA), and the Coronavirus Aid, Relief, and Economic Security Act, Public Law 116–136 (2020) (CARES Act). Section 13301(a) of the TCJA amended section 163(j) by removing prior section 163(j)(1) through (9) and adding section 163(j)(1) through (10). The provisions of section 163(j) as amended by section 13301 of the TCJA are effective for tax years beginning after December 31, 2017. The CARES Act further amended section 163(j) by redesignating section 163(j)(10), as amended by the TCJA, as new section 163(j)(11), and adding a new section 163(j)(10) providing special rules for applying section 163(j) to taxable years beginning in 2019 or 2020.

Section 163(j) generally limits the amount of business interest expense (BIE) that can be deducted in the current taxable year (also referred to in this Preamble as the current year). Under section 163(j)(1), the amount allowed as a deduction for BIE is limited to the sum of (1) the taxpayer's business interest income (BII) for the taxable year; (2) 30 percent of the taxpayer's adjusted taxable income (ATI) for the taxable year (30 percent ATI limitation); and (3) the taxpayer's floor plan financing interest expense for the taxable year (in sum, the section 163(j) limitation). As further described later in this Background section, section 163(j)(10), as amended by the CARES Act, provides special rules relating to the ATI limitation for taxable years beginning in 2019 or 2020. Under section 163(j)(2), the amount of any BIE that is not allowed as a deduction in a taxable year due to the section 163(j) limitation is treated as business interest paid in the succeeding taxable year.

The section 163(j) limitation applies to all taxpayers, except for certain small businesses that meet the gross receipts test in section 448(c) and certain trades or businesses listed in section 163(j)(7). Section 163(j)(3) provides that the section 163(j) limitation does not apply to any taxpayer that meets the gross receipts test under section 448(c), other than a tax shelter prohibited from using the cash receipts and disbursements method of accounting under section 448(a)(3).

Section 163(j)(4) provides special rules for applying section 163(j) in the case of passthrough entities. Section 163(j)(4)(A) requires that the section 163(j) limitation be applied at the partnership level, and that a partner's ATI be increased by the partner's share of excess taxable income, as defined in section 163(j)(4)(C), but not by the partner's distributive share of income, gain, deduction, or loss. Section 163(j)(4)(B) provides that the amount of partnership BIE limited by section 163(j)(1) (EBIE) is carried forward at the partner level. Section 163(j)(4)(B)(ii) provides that EBIE allocated to a partner and carried forward is available to be deducted in a subsequent year only to the extent that the partnership allocates excess taxable income to the partner. As further described later in this Background section, section 163(j)(10), as amended by the CARES Act, provides a special rule for excess business interest expense allocated to a partner in a taxable year beginning in 2019.

Section 163(j)(4)(B)(iii) provides rules for the adjusted basis in a partnership of a partner that is allocated EBIE. Section 163(j)(4)(D) provides that rules similar to the rules of section 163(j)(4)(A) and (C) apply to S corporations and S corporation shareholders.

Section 163(j)(5) and (6) define ''business interest'' and ''business interest income,'' respectively, for purposes of section 163(j). Generally, these terms include interest expense and interest includible in gross income that is properly allocable to a trade or business (as defined in section 163(j)(7)) and do not include investment income or investment expense within the meaning of section 163(d). The legislative history states that ''a corporation has neither investment interest nor investment income within the meaning of section 163(d). Thus, interest income and interest expense of a corporation is properly allocable to a trade or business, unless such trade or business is otherwise explicitly excluded from the application of the provision.'' H. Rept. 115–466, at 386, fn. 688 (2017).

Under section 163(j)(7), the limitation on the deduction for business interest expense in section 163(j)(1) does not apply to certain trades or businesses (excepted trades or businesses). The excepted trades or businesses are the trade or business of providing services as an employee, electing real property businesses, electing farming businesses, and certain regulated utility businesses.

Section 163(j)(8) defines ATI as the taxable income of the taxpayer without regard to the following: Items not properly allocable to a trade or business; business interest and business interest income; net operating loss (NOL) deductions; and deductions for qualified business income under section 199A. ATI also generally excludes deductions for depreciation, amortization, and depletion with respect to taxable years beginning before January 1, 2022, and it includes other adjustments provided by the Secretary of the Treasury.

Section 163(j)(9) defines ''floor plan financing interest'' as interest paid or accrued on ''floor plan financing indebtedness.'' These provisions allow taxpayers incurring interest expense for the purpose of securing an inventory of motor vehicles held for sale or lease to deduct the full expense without regard to the section 163(j) limitation.

Under section 163(j)(10)(A)(i), the amount of business interest that is deductible under section 163(j)(1) for taxable years beginning in 2019 or 2020 is computed using 50 percent, rather than 30 percent, of the taxpayer's ATI for the taxable year (50 percent ATI limitation). A taxpayer may elect not to apply the 50 percent ATI limitation to any taxable year beginning in 2019 or 2020, and instead apply the 30 percent ATI limitation. This election must be made separately for each taxable year. Once the taxpayer makes the election, the election may not be revoked without the consent of the Secretary of the Treasury or his delegate. See section 163(j)(10)(A)(iii).

Sections 163(j)(10)(A)(ii)(I) and 163(j)(10)(A)(iii) provide that, in the case of a partnership, the 50 percent ATI limitation does not apply to partnerships for taxable years beginning in 2019, and the election to not apply the 50 percent ATI limitation may be made only for taxable years beginning in 2020, and may be made only by the partnership. Under section 163(j)(10)(A)(ii)(II), however, a partner treats 50 percent of its allocable share of a partnership's excess business interest expense for 2019 as a business interest expense in the partner's first taxable year beginning in 2020 that is not subject to the section 163(j) limitation (50 percent EBIE rule). The remaining 50 percent of the partner's allocable share of the partnership's excess business interest expense remains subject to the section 163(j) limitation applicable to excess business interest expense carried forward at the partner level. A partner may elect out of the 50 percent EBIE rule.

Section 163(j)(10)(B)(i) allows a taxpayer to elect to substitute its ATI for the last taxable year beginning in 2019 (2019 ATI) for the taxpayer's ATI for a taxable year beginning in 2020 (2020 ATI) in determining the taxpayer's section 163(j) limitation for the taxable year beginning in 2020.

Section 163(j)(11) provides cross-references to provisions requiring that electing farming businesses and electing real property businesses excepted from the section 163(j) limitation use the alternative depreciation system (ADS), rather than the general depreciation system, for certain types of property. The required use of ADS results in the inability of these electing trades or businesses to use the additional first-year depreciation deduction under section 168(k) for those types of property.

On December 28, 2018, the Department of the Treasury (Treasury Department) and the IRS (1) published proposed regulations under section 163(j), as amended by the TCJA, in a notice of proposed rulemaking (REG–106089–18) (2018 Proposed Regulations) in the **Federal Register** (83 FR 67490), and (2) withdrew the notice of proposed rulemaking (1991–2 C.B. 1040) published in the **Federal Register** on June 18, 1991 (56 FR 27907 as corrected by 56 FR 40285 (August 14, 1991)) to implement rules under section 163(j) before amendment by the TCJA. The 2018 Proposed Regulations were issued following guidance announcing and describing regulations intended to be issued under section 163(j). See Notice 2018–28, 2018–16 I.R.B. 492 (April 16, 2018).

A public hearing on the 2018 Proposed Regulations was held on February 27, 2019. The Treasury Department and the IRS also received written comments responding to the 2018 Proposed Regulations (available at *http://www.regulations.gov*). In response to certain comments, the Treasury Department and the IRS are publishing this notice of proposed rulemaking to provide additional proposed regulations (these Proposed Regulations) under section 163(j).

Concurrently with the publication of these Proposed Regulations, the Treasury Department and the IRS are publishing in the Rules and Regulations section of this edition of the **Federal Register** (RIN 1545–BO73) final regulations under section 163(j) (the Final Regulations).

On April 10, 2020, the Treasury Department and the IRS released Revenue Procedure 2020–22, 2020–18 I.R.B. 745, to provide the time and manner of making a late election, or withdrawing an election, under section 163(j)(7)(B) to be an electing real property trade or business or section 163(j)(7)(C) to be an electing farming business for taxable years beginning in 2018, 2019, or 2020. Revenue Procedure 2020–22 also provides the time and manner of making or revoking elections provided by the CARES Act under section 163(j)(10) for taxable years beginning in 2019 or 2020. As described earlier in this Background section, these elections are: (1) To not apply the 50 percent ATI limitation under section 163(j)(10)(A)(iii); (2) to use the taxpayer's 2019 ATI to calculate the taxpayer's section 163(j) limitation for any taxable year beginning in 2020 under section 163(j)(10)(B); and (3) for a partner to elect out of the 50 percent EBIE rule under section 163(j)(10)(A)(ii)(II).

Explanation of Provisions

These Proposed Regulations would provide guidance in addition to the Final Regulations regarding the section 163(j) limitation. These Proposed Regulations would also add or amend regulations under certain other provisions of the Code where necessary to provide conformity across the Income Tax Regulations. A significant number of the terms used throughout these Proposed Regulations are defined in § 1.163(j)–1 of the Final Regulations and discussed in the Explanation of Provisions section of the 2018 Proposed Regulations and the Summary of Comments and Explanation of Revisions section of the Final Regulations. Some of these terms are further discussed in this Explanation of Provisions section as they relate to specific provisions of these Proposed Regulations.

Part I of this Explanation of Provisions describes proposed rules that would allocate interest expense for purposes of sections 469, 163(d), 163(h), and 163(j) in connection with certain transactions involving passthrough entities. Part II provides proposed rules relating to distributions of debt proceeds from any taxpayer account or from cash so that interest expense may be allocated for purposes of sections 469, 163(d), 163(h), and 163(j). Part III describes proposed modifications to the definitions and general guidance in § 1.163(j)–1, including proposed rules permitting taxpayers to apply a different computational method in determining adjustments to tentative taxable income to address sales or other dispositions of depreciable property, stock of a consolidated group member, or interests in a partnership, and proposed rules allowing RIC shareholders to treat certain RIC dividends as interest income for purposes of section 163(j). Part IV describes proposed modifications to § 1.163(j)–6, relating to the applicability of the section 163(j) limitation to passthrough entities, including proposed rules on the applicability of the section 163(j) limitation to trading partnerships and publicly traded partnerships, the application of the section 163(j) limitation in partnership self-charged lending transactions, proposed rules relating to the treatment of excess business interest expense in tiered partnerships, proposed rules relating to partnership basis adjustments upon partner dispositions, proposed rules regarding the election to substitute 2019 ATI for the partnership's 2020 ATI in determining the partnership's section 163(j) limitation for a taxable year beginning in 2020, and proposed rules regarding excess business interest expense allocated to a partner in a taxable year beginning in 2019.

Part V discusses re-proposed rules regarding the application of the section 163(j) limitation to foreign corporations and United States shareholders (as defined in section 951(b) (U.S. shareholders) of controlled foreign corporations (as defined in section 957(a)) (CFCs). Part VI discusses re-proposed rules regarding the application of the section 163(j) limitation to nonresident alien individuals and foreign corporations with effectively connected income in the United States. Part VII describes proposed modifications to the definition of a real property trade or business under § 1.469–9 for purposes of the passive activity loss rules and the definition of an electing real property trade or business under section 163(j)(7)(B). Part VIII describes proposed rules regarding the definition of a ''tax shelter'' for purposes of § 1.163(j)–2 and section 1256(e), as well as proposed rules regarding the election to use 2019 ATI in determining the taxpayer's section 163(j) limitation for a taxable year beginning in 2020. Part IX describes proposed modifications regarding the application of the corporate look-through rules to tiered structures.

I. Proposed § 1.163–14: Allocation of Interest Expense With Respect to Passthrough Entities

Section 1.163–8T provides rules regarding the allocation of interest expense for purposes of applying the passive activity loss limitation in section 469, the investment interest limitation in section 163(d), and the personal interest limitation in section 163(h) (such purposes, collectively, § 1.163–8T purposes). Under § 1.163–8T, debt generally is allocated by tracing disbursements of the debt proceeds to specific expenditures and interest expense associated with debt is allocated for § 1.163–8T purposes in the same manner as the debt to which such interest expense relates. When debt proceeds are deposited to the borrower's account, and the account also contains unborrowed funds, § 1.163–8T(c) provides that the debt generally is allocated to expenditures by treating subsequent expenditures from the account as made first from the debt proceeds to the extent thereof. The rules further provide that if the proceeds of two or more debts are deposited in the account, the proceeds are treated as expended in the order in which they were deposited. In addition to these rules, § 1.163–8T also provides specific rules to address reallocation of debt, repayments and refinancing.

The preamble to § 1.163–8T (52 FR 24996) stated that ''interest expense of partnerships and S corporations, and of partners and S corporation shareholders, is generally allocated in the same manner as the interest expense of other taxpayers.'' The preamble acknowledged the need for special rules for debt financed distributions to owners of partnerships and S corporations, and for cases in which taxpayers incur debt to acquire or increase their capital interest in the passthrough entity, but reserved on these issues and requested comments.

In a series of notices, the Treasury Department and the IRS provided further guidance with respect to the allocation of interest expense in connection with certain transactions involving passthrough entities and owners of passthrough entities. See Notice 88–20, 1988–1 C.B. 487, Notice 88–37, 1988–1 C.B. 522, and Notice 89–35, 1989–1 C.B. 675. Specifically, Notice 89–35 provides, in part, rules addressing the treatment of (1) a passthrough entity owner's debt allocated to contributions to, or purchases of, interests in a passthrough entity (debt-financed contributions or acquisitions), and (2) passthrough entity debt allocated to distributions by the entity to its owners (debt-financed distributions).

In the case of a debt-financed acquisition of an interest in a passthrough entity by purchase (rather than by way of a contribution to the capital of the entity), Notice 89–35 provides that the interest expense of the owner of the passthrough entity, for § 1.163–8T purposes, is allocated among the assets of the entity using any reasonable method. A reasonable method for this purpose includes, for example, allocating the debt among all of the assets of the passthrough entity based on the fair market value, the book value, or the adjusted basis of the assets, reduced by the amount of any debt of the entity or the amount of any debt that the owner of the entity allocates to such assets. Notice 89–35 also provides that interest expense on debt proceeds allocated to a contribution to the capital of a passthrough entity shall be allocated using any reasonable method for § 1.163–8T purposes. For this purpose, any reasonable method includes allocating the debt among the assets of the passthrough entity or tracing the debt proceeds to the expenditures of the passthrough entity.

In the case of debt-financed distributions, Notice 89–35 provides a general allocation rule and an optional allocation rule. The general allocation rule applies the principles of § 1.163–8T to interest expense associated with debt-financed distributions by applying a tracing approach to determine the character of the interest expense for § 1.163–8T purposes. Under this approach, the debt proceeds and the associated interest expense related to a debt-financed distribution are allocated under § 1.163–8T in accordance with the use of the distributed debt proceeds by the distributee owner of the passthrough entity. To the extent an owner's share of a passthrough entity's interest expense related to the debt-financed distribution exceeds the entity's interest expense on the portion of the debt proceeds distributed to that particular owner, Notice 89–35 provides that the passthrough entity may allocate such excess interest expense using any reasonable method.

The optional allocation rule applicable to debt-financed distributions allows a passthrough entity to allocate distributed debt proceeds and the associated interest expense to one or more expenditures, other than distributions, of the entity that are made during the same taxable year of the entity as the distribution, to the extent that debt proceeds, including other distributed debt proceeds, are not otherwise allocated to such expenditures. Under the optional allocation rule, distributed debt proceeds are traced to the owner's use of the borrowed funds to the extent that such distributed debt proceeds exceed the entity's expenditures, not including distributions, for the taxable year to which debt proceeds are not otherwise allocated.

While the 2018 Proposed Regulations did not include rules to further address the application of § 1.163–8T to passthrough entities, the Treasury Department and the IRS received comments indicating that, for purposes of section 163(j), a tracing rule based on how a passthrough entity owner uses the proceeds of a debt-financed distribution does not align well with the statutory mandate in section 163(j)(4) to apply section 163(j) at the passthrough entity level. Based on these comments and a review of the rules under § 1.163–8T, the Treasury Department and the IRS have determined that additional rules, specific to passthrough entities and their owners, are needed to clarify how the rules under § 1.163–8T work when applied to a passthrough entity and to account for the entity-level limitation under section 163(j)(4).

A. In General

The rules of § 1.163–8T generally apply to partnerships, S corporations, and their owners and the rules in proposed § 1.163–14 would provide additional rules for purposes of applying the § 1.163–8T rules to passthrough entities. As with the rules under § 1.163–8T, proposed § 1.163–14 would provide that interest expense on a debt incurred by a passthrough entity is allocated in the same manner as the debt to which such interest relates is allocated, and that debt is generally allocated by tracing disbursements of the debt proceeds to specific expenditures.

The Treasury Department and the IRS have determined that the scope of § 1.163–8T(a)(4) and (b) is not appropriate in the passthrough entity context. Section 1.163–8T(a)(4) generally provides rules regarding the treatment of interest expense allocated to specific expenditures, which are described in § 1.163–8T(b). However, the list of expenditures described in § 1.163–8T(b) is based on an allocation of interest for purposes of applying sections 163(d), 163(h), and 469, and does not adequately account for the uses of debt proceeds by a passthrough entity (for example, distributions to owners).

To more accurately account for the types of expenditures made by passthrough entities, proposed § 1.163–14(b) would provide rules tailored to passthrough entities. In addition, the framework that proposed § 1.163–14(b) would provide is needed for a passthrough entity to determine how much of its interest expense is allocable to a trade or business for purposes of applying section 163(j). These proposed regulations would apply before a passthrough entity applies any of the rules in section 163(j) (including § 1.163(j)–10).

In application, a passthrough entity would continue to apply the operative rules in § 1.163–8T to allocate debt and the interest expense associated with such debt. However, instead of generally tracing debt proceeds to the types of expenditures described under § 1.163–8T(b) and treating any interest expense associated with such debt proceeds in the manner described under § 1.163–8T(a)(4), a passthrough entity would generally trace debt proceeds to the types of expenditures described under proposed § 1.163–14(b)(2) and treat any interest expense associated with such debt proceeds in the manner provided under proposed § 1.163–14(b)(1).

B. Debt Financed Distributions

Proposed § 1.163–14 would provide that when debt proceeds of a passthrough entity are allocated under § 1.163–8T to distributions to owners of the entity, the debt proceeds distributed to any owner and the associated interest expense shall be allocated under proposed § 1.163–14(d). In general, proposed § 1.163–14(d) would adopt a rule similar to Notice 89–35, but with the following modifications. First, instead of providing that passthrough entities may use the optional allocation rule, proposed § 1.163–14(d) would generally provide that passthrough entities are required to apply a rule that is similar to the optional allocation rule. Second, instead of providing that the passthrough entity may allocate excess interest expense using any reasonable method, proposed § 1.163–14(d) would generally provide that the passthrough entity must allocate excess interest expense based on the adjusted tax basis of the passthrough entity's assets.

Specifically, proposed § 1.163–14(d)(1) would provide a rule based in principle on the optional allocation rule in Notice 89–35. Under this proposed rule, distributed debt proceeds (debt proceeds of a passthrough entity allocated under § 1.163–8T to distributions to owners of the entity) would first be allocated under proposed § 1.163–14(d)(1)(i) to the passthrough entity's available expenditures. Available expenditures are those expenditures of a passthrough entity made in the same taxable year as the distribution, but only to the extent that debt proceeds (including other distributed debt proceeds) are not otherwise allocated to such expenditure. This approach is consistent with the concept that money is fungible (a passthrough entity may be fairly treated as distributing non-debt proceeds rather than debt proceeds and using debt proceeds rather than non-debt proceeds to finance its non-distribution expenditures) and seeks to coordinate the interest allocation rules with the entity-level approach to passthroughs adopted in section 163(j). Where the distributed debt proceeds exceed the passthrough entity's available expenditures, this excess amount of distributed debt proceeds would be allocated to distributions to owners of the passthrough entity (debt financed distributions) under proposed § 1.163–14(d)(1)(ii).

After determining the amount of its distributed debt proceeds allocated to available expenditures and debt financed distributions, a passthrough entity would use this information to determine the tax treatment of each owner's allocable interest expense (that is, an owner's share of interest expense associated with the distributed debt proceeds allocated under section 704(b) or 1366(a)). To aid the passthrough entity and owner in determining the tax treatment of each owner's allocable interest expense, proposed § 1.163–14(d)(2) would provide rules for determining the portion of each owner's allocable interest expense that is (1) debt financed distribution interest expense, (2) expenditure interest expense, and (3) excess interest expense. These three categories of allocable interest expense are mutually exclusive—*e.g.,* a given dollar of allocable interest expense cannot simultaneously be both debt financed distribution interest expense and expenditure interest expense. The computations in proposed § 1.163–14(d)(2) would ensure this outcome.

Once a passthrough entity categorizes each owner's allocable interest expense as described earlier, it would apply proposed § 1.163–14(d)(3) to determine the tax treatment of such interest expense. The manner in which the tax treatment of allocable interest expense is determined depends on how such allocable interest expense was categorized under proposed § 1.163–14(d)(2).

Conceptually, each of the three categories described earlier, as well as the prescribed tax treatment of interest expense in each category, is discussed in Notice 89–35. Debt financed distribution interest expense is referred to in Notice 89–35 as an owner's share of a passthrough entity's interest expense on debt proceeds allocated to such owner. Similar to Notice 89–35, proposed § 1.163–14(d)(3)(i) would generally provide that such interest expense is allocated under § 1.163–8T in accordance with the owner's use of the debt proceeds. Further, expenditure interest expense is referred to in Notice 89–35 as interest expense allocated under the optional allocation rule. Similar to Notice 89–35, proposed § 1.163–14(d)(3)(ii) would generally provide that the tax treatment of such interest expense is determined based on how the distributed debt proceeds were allocated among available expenditures. Finally, both Notice 89–35 and proposed § 1.163–14(d) would use the term excess interest expense to refer to an owner's share of allocable interest expense in excess of the entity's interest expense on the portion of the debt proceeds distributed to that particular owner. Unlike Notice 89–35, which generally allows any reasonable method for determining the tax treatment of excess interest expense, proposed § 1.163–14(d)(3)(iii) would generally provide that the tax treatment of excess interest expense is determined by allocating the distributed debt proceeds among all the assets of the passthrough entity, pro-rata, based on the adjusted basis of such assets.

Proposed § 1.163–14(d)(4) also would provide rules addressing the tax treatment of the interest expense of a transferee owner where the transferor had previously been allocated debt financed distribution interest expense. In the case of a transfer of an interest in a passthrough entity, any debt financed distribution interest expense of the transferor generally shall be treated as excess interest expense by the transferee. However, in the case of a transfer of an interest in a passthrough entity to a person who is related to the transferor, any debt financed distribution interest expense of the transferor shall continue to be treated as debt financed distribution interest expense by the related party transferee, and the tax treatment of such debt financed distribution expense shall be the same to the related party transferee as it was to the transferor. The term related party means any person who bears a relationship to the taxpayer which is described in section 267(b) or 707(b)(1).

The proposed regulations also would include an anti-avoidance rule to recharacterize arrangements entered into with a principal purpose of avoiding the rules of proposed § 1.163–14(d), including the transfer of an interest in a passthrough entity by an owner who treated a portion of its allocable interest expense as debt financed distribution interest expense to an unrelated party pursuant to a plan to transfer the interest back to the owner who received the debt financed distribution interest expense or to a party who is related to the owner who received the debt financed distribution interest expense.

C. Operational Rules

Proposed § 1.163–14 also would include several operational rules that clarify the application of certain rules under § 1.163–8T as they apply to passthrough entities. Proposed § 1.163–14(e) would provide an ordering rule applicable to repayment of debt by passthrough entities similar to the rules in § 1.163–8T(d)(1). Proposed § 1.163–14(g) would provide that any transfer of an ownership interest in a passthrough entity is not a reallocation event for purposes of § 1.163–8T(j), except as provided for in § 1.163–14(d)(4).

D. Debt-Financed Acquisitions

Proposed § 1.163–14(f) would adopt a rule providing that the tax treatment of an owner's interest expense associated with a debt financed acquisition (either by purchase or contribution) will be determined by allocating the debt proceeds among the assets of the entity. The owner would allocate the debt proceeds (1) in proportion to the relative adjusted tax basis of the entity's assets reduced by any debt allocated to such assets, or (2) based on the adjusted basis of the entity's assets in accordance with the rules in § 1.163(j)–10(c)(5)(i) reduced by any debt allocated to such assets. The Treasury Department and the IRS request comments regarding whether asset basis (either adjusted tax basis or adjusted tax basis based on the rules in § 1.163(j)–10(c)(5)(i)) less the amount of debt allocated to assets under §§ 1.163–14 and 1.163–8T is appropriate as the sole method for allocating interest expense in this context.

II. Proposed § 1.163–15: Debt Proceeds Distributed From Any Taxpayer Account or From Cash

Proposed § 1.163–15 supplements the rules in § 1.163–8T regarding debt proceeds distributed from any taxpayer account or from cash proceeds. Section 1.163–8T(c)(4)(iii)(B) provides that a taxpayer may treat any expenditure made from an account within 15 days after the debt proceeds are deposited in such account as being made from such proceeds, regardless of any other rules in § 1.163–8T(c)(4). Under § 1.163–8T(c)(5)(i), if a taxpayer receives debt proceeds in cash, the taxpayer may treat any cash expenditure made within 15 days after receiving the cash as being made from such debt proceeds, and may treat such expenditure as being made on the date the taxpayer received the cash. Commenters have suggested that the 15-day limit in § 1.163–8T could encourage taxpayers to keep separate accounts, rather than commingled accounts for tracing purposes.

In Notice 88–20, 1988–1 C.B. 487, the IRS announced the intention to issue regulations providing that, for debt proceeds deposited in an account on or before December 31, 1987, taxpayers could treat any expenditure made from any account of the taxpayer or from cash within 30 days before or after debt proceeds are deposited in such account or any other account of the taxpayer as made from such proceeds. The Notice states that the regulations also would provide that for debt proceeds received in cash on or before December 31, 1987, taxpayers may treat any expenditure made from any account of the taxpayer or from cash within 30 days before or after debt proceeds are received in cash as made from such proceeds. Section VI of Notice 89–35 adopts the standard described in Notice 88–20 without the date limitation, although no regulations have been issued.

Consistent with Notice 89–35, proposed § 1.163–15 provides that taxpayers may treat any expenditure made from an account of the taxpayer or from cash within 30 days before or after debt proceeds are deposited in any account of the taxpayer or received in cash as made from such proceeds.

III. Proposed Modifications to § 1.163(j)–1(b): Definitions

A. Adjustments to Tentative Taxable Income

Section 1.163(j)–1(b)(1) requires taxpayers to make certain adjustments to tentative taxable income in computing ATI, including adjustments to address certain sales or other dispositions of depreciable property, stock of a consolidated group member (member stock), or interests in a partnership. More specifically, § 1.163(j)–1(b)(1)(ii)(C) provides that, if property is sold or otherwise disposed of, the greater of the allowed or allowable depreciation, amortization, or depletion of the property for the taxpayer (or, if the taxpayer is a member of a consolidated group, the consolidated group) for taxable years beginning after December 31, 2017, and before January 1, 2022 (such years, the EBITDA period), with respect to such property is subtracted from tentative taxable income. Section 1.163(j)–1(b)(1)(ii)(D) provides that, with respect to the sale or other disposition of stock of a member of a consolidated group by another member, the investment adjustments under § 1.1502–32 with respect to such stock that are attributable to deductions described in § 1.163(j)–1(b)(1)(ii)(C) are subtracted from tentative taxable income. Section 1.163(j)–1(b)(1)(ii)(E) provides that, with respect to the sale or other disposition of an interest in a partnership, the taxpayer's distributive share of deductions described in § 1.163(j)–1(b)(1)(ii)(C) with respect to property held by the partnership at the time of such sale or other disposition is subtracted from tentative taxable income to the extent such deductions were allowable under section 704(d). See the preamble to the Final Regulations for a discussion of the rationale for these adjustments.

The preamble to the Final Regulations noted that, in the 2018 Proposed Regulations, § 1.163(j)–1(b)(1)(ii)(C) incorporated a ''lesser of'' standard. In other words, the lesser of (i) the amount of gain on the sale or other disposition of property, or (ii) the amount of depreciation deductions with respect to such property for the EBITDA period, was required to be subtracted from tentative taxable income to determine ATI. As explained in the preamble to the Final Regulations, commenters raised several questions regarding this ''lesser of'' standard. The Final Regulations removed the ''lesser of'' approach due in part to concerns that this approach would be more difficult to administer than the approach reflected in the Final Regulations.

However, the Treasury Department and the IRS recognize that, in certain cases, the ''lesser of'' approach might not create administrative difficulties for taxpayers. Thus, these Proposed Regulations permit taxpayers to choose whether to compute the amount of their adjustment using a ''lesser of'' standard. While the 2018 Proposed Regulations applied this standard solely to dispositions of property, these Proposed Regulations extend this standard to dispositions of partnership interests and member stock to eliminate the discontinuity between the amount of the adjustment for these different types of dispositions. Taxpayers opting to use this alternative computation method must do so for all sales or other dispositions that otherwise would be subject to § 1.163(j)–1(b)(1)(ii)(C), (D), or (E) when the taxpayer computes tentative taxable income.

The Treasury Department and the IRS request comments on the ''lesser of'' approach, including how such an approach should apply to dispositions of member stock and partnership interests.

B. Dividends From Regulated Investment Company (RIC) Shares

Some commenters on the 2018 Proposed Regulations recommended that dividend income from a RIC be treated as interest income for a shareholder in a RIC, to the extent that the income earned by the RIC is interest income. Because a RIC is a subchapter C corporation, section 163(j) applies at the RIC level, and any BIE that is disallowed at the RIC level is carried forward to subsequent years at the RIC level. Furthermore, because a RIC is a subchapter C corporation, a shareholder in a RIC generally does not take into account a share of the RIC's items of income, deduction, gain, or loss. Thus, if a RIC's BII exceeds its BIE in a taxable year, the RIC may not directly allocate the excess amount to its shareholders (unlike a partnership, which may allocate excess BII to its partners).

Under part 1 of subchapter M and other Code provisions, however, a RIC that has certain items of income or gain may pay dividends that a shareholder in the RIC may treat in the same manner (or a similar manner) as the shareholder would treat the underlying items of income or gain if the shareholder realized the items directly. Although this treatment differs fundamentally from the passthrough treatment of partners or trust beneficiaries, this Explanation of Provisions refers to this treatment as ''conduit treatment.'' For example, under sections 871(k)(1) and 881(e)(1), a RIC that has qualified interest income within the meaning of section 871(k)(1)(E) may pay interest-related dividends, and no tax generally would be imposed under sections 871(a)(1)(A) or 881(a)(1) on an interest-related dividend paid to a nonresident alien individual or foreign corporation. Section 871(k)(1) provides necessary limits and procedures that apply to interest-related dividends. The Code provides similar conduit treatment for capital gain dividends in section 852(b)(3), exempt-interest dividends in section 852(b)(5), short-term capital gain dividends in section 871(k)(2), dividends eligible for the dividends received deduction in section 854(b)(1)(A), and qualified dividend income in section 854(b)(1)(B).

In response to comments, these Proposed Regulations provide rules under which a RIC that earns BII may pay section 163(j) interest dividends. A shareholder that receives a section 163(j) interest dividend may treat the dividend as interest income for purposes of section 163(j), subject to holding period requirements and other limitations. A section 163(j) interest dividend that meets these requirements is treated as BII if it is properly allocable to a non-excepted trade or business of the shareholder. A section 163(j) interest dividend is treated as interest income solely for purposes of section 163(j).

The rules under which a RIC may report section 163(j) interest dividends are based on the rules for reporting exempt-interest dividends in section 852(b)(5) and interest-related dividends in section 871(k)(1). The total amount of a RIC's section 163(j) interest dividends for a taxable year is limited to the excess of the RIC's BII for the taxable year over the sum of the RIC's BIE for the taxable year and the RIC's other deductions for the taxable year that are properly allocable to the RIC's BII. For some types of income and gain to which conduit treatment applies, the gross amount of the RIC's income or gain of that type serves as the limit on the RIC's corresponding dividends. It would be inconsistent with the purposes of section 163(j) to permit a RIC to pay section 163(j) interest dividends in an amount based on the RIC's gross BII, unreduced by the RIC's BIE. Further reducing the limit on a RIC's section 163(j) interest dividends by the amount of the RIC's other deductions that are properly allocable to the RIC's BII is consistent with the provisions of the Code that provide conduit treatment for types of interest earned by a RIC. For example, the limit on interest-related dividends in section 871(k)(1)(D) is reduced by the deductions properly allocable to the RIC's qualified interest income. Similarly, the limit on exempt-interest dividends in section 852(b)(5)(A)(iv)(V) is reduced by the amounts disallowed as deductions under sections 265 and 171(a)(2). Taking into account the appropriate share of deductions also reduces the likelihood that the sum of a RIC's items that are eligible for conduit treatment and that are relevant to a particular shareholder will exceed the amount of the dividend distribution paid to the particular shareholder.

These Proposed Regulations contain an additional limit to prevent inconsistent treatment of RIC dividends by RIC shareholders. Revenue Ruling 2005–31, 2005–1 C.B. 1084, allows a RIC to report the maximum amount of capital gain dividends, exempt-interest dividends, interest-related dividends, short-term capital gain dividends, dividends eligible for the dividends received deduction, and qualified dividend income for a taxable year, even if the sum of the reported amounts exceeds the amount of the RIC's dividends for the taxable year. The ruling allows different categories of shareholders (United States persons and nonresident aliens) to report the dividends they receive by giving effect to the conduit treatment of the items relevant to them. A single shareholder, however, generally does not benefit from the conduit treatment of amounts in excess of the dividend paid to that shareholder, because to do so would require the shareholder to include in its taxable income amounts exceeding the dividend it received. Conduit treatment of BII, however, differs from the conduit treatment of other items, because a section 163(j) interest dividend is treated as interest income only for purposes of section 163(j). Thus, absent a limit, a RIC shareholder could obtain an inappropriate benefit by treating a portion of a RIC dividend as interest income for purposes of section 163(j) while treating the same portion of the dividend as another non-interest type of income, such as a dividend eligible for the dividends received deduction under sections 243 and 854(b). Therefore, these Proposed Regulations limit the amount of a section 163(j) interest dividend that a shareholder may treat as interest income for purposes of section 163(j) to the excess of the amount of the RIC dividend that includes the section 163(j) interest dividend over the sum of the portions of that dividend affected by conduit treatment in the hands of that shareholder, other than interest-related dividends under section 871(k)(1)(C) and section 163(j) interest dividends.

Under these Proposed Regulations, a shareholder generally may not treat a section 163(j) interest dividend as interest income unless it meets certain holding period and similar requirements. The holding period requirements do not apply to (i) dividends paid by a RIC regulated as a money market fund under 17 CFR 270.2a–7 or (ii) certain regular dividends paid by a RIC that declares section 163(j) interest dividends on a daily basis and distributes such dividends on a monthly or more frequent basis. The Treasury Department and the IRS request comments on whether there are other categories of section 163(j) interest dividends for which the holding period requirements should not apply or should be modified. The Treasury Department and the IRS also request comments on whether any payments that are substitutes for section 163(j) interest dividends (for example, in a securities lending or sale-repurchase transaction with respect to RIC shares) should be treated for purposes of section 163(j) as interest expense of taxpayers making the payments or interest income to taxpayers receiving the payments. Cf. § 1.163(j)–1(b)(22)(iii)(C) (addressing certain payments that are substitutes for interest).

These Proposed Regulations, to the extent they concern the payment of section 163(j) interest dividends by a RIC and the treatment of such dividends as interest by a RIC shareholder, are proposed to apply to taxable years beginning on or after the date that is 60 days after the date the Treasury decision adopting these regulations as final regulations is published in the **Federal Register**. Solely in the case of section 163(j) interest dividends that would be exempt from the holding period rules under these Proposed Regulations, the RIC paying such dividends and the shareholders receiving such dividends may rely on the provisions of these Proposed Regulations pertaining to section 163(j) interest dividends for taxable years ending on or after September 14, 2020, and beginning before the date that is 60 days after the date the Treasury decision adopting these regulations as final regulations is published in the **Federal Register**.

IV. Proposed § 1.163(j)–6: Application of the Business Interest Expense Deduction Limitations to Partnerships and Subchapter S Corporations

A. Trading Partnerships

The preamble to the 2018 Proposed Regulations states that the business interest expense of certain passthrough entities, including S corporations, allocable to trade or business activities that are described in section 163(d)(5)(A)(ii) (*i.e.,* activities that are per se non-passive under section 469 in which the taxpayer does not materially participate) and illustrated in Revenue Ruling 2008–12, 2008–1 C.B. 520 (March 10, 2008) (trading activities), will be subject to section 163(j) at the entity level, even if the interest expense is later subject to limitation under section 163(d) at the individual partner or shareholder level. Accordingly, at least with respect to partnerships, to the extent that interest expense from a trading activity is limited under section 163(j) and becomes a carryover item of partners who do not materially participate in the trading activity, the interest expense will be treated as investment interest in the hands of those partners for purposes of section 163(d) once the interest expense is no longer limited under section 163(j). As a result, the interest expense would be subject to two section 163 limitations.

The Treasury Department and the IRS received multiple comments questioning this interpretation of section 163(j)(5) and its interaction with section 163(d)(5)(A)(ii). Specifically, commenters stated that the interpretation improperly results in the application of section 163(j) to partnerships engaged in a trade or business activity of trading personal property (including marketable securities) for the account of owners of interests in the activity, as described in § 1.469–1T(e)(6) (trading partnerships). At issue is the extent to which BIE of trading partnerships should be subject to limitation under section 163(j). This issue involves the definition of BIE under section 163(j)(5) and, more specifically, the second sentence of section 163(j)(5), which generally provides that BIE shall not include investment interest within the meaning of section 163(d).

The approach described in the preamble to the 2018 Proposed Regulations interprets section 163(j)(5) as simply providing that interest expense cannot be both BIE and investment interest expense in the hands of the same taxpayer. Under this interpretation, section 163(j)(5) will treat interest as investment interest where conflicting provisions may otherwise subject an amount of interest expense to limitation under both section 163(j) and section 163(d) with respect to the same taxpayer (for example, interest expense allocable to business assets comprising ''working capital'' as that term is used in section 469(e)(1)(B)). In addition, this approach views the partnership as an entity separate from its partners for purposes of section 163(j) to the partnership and section 163(d) at the individual partner level. Several commenters disagreed with this interpretation of section 163(j)(5), asserting that the second sentence of section 163(j)(5) unequivocally provides that interest expense can never be subject to limitation under both section 163(j) and section 163(d) under any circumstances. Based on these comments, the Treasury Department and the IRS considered three alternative approaches for interpreting section 163(j)(5).

One approach would require a partnership engaged in a trading activity to apply section 163(j) at the partnership level to all of the partnership's interest expense from the trading activity. Under this approach, any deductible interest expense from the partnership's trading activity would not be subject to any further limitation under section 163(d) at the individual partner level. This interpretation would respect the partnership as an entity separate from its partners for purposes of section 163(j), but would treat section 163(j)(4) and (5) as superseding section 163(d)(5)(A)(ii).

A second approach would require a partnership engaged in a trading activity to bifurcate its interest expense from a trading activity between partners that materially participate in the trading activity and partners that are passive investors in the activity, and subject only the portion that is allocable to the materially participating partners to limitation under section 163(j). Under this approach, to the extent any interest expense is allocable to passive investors in the trading activity, the interest expense would be subject only to section 163(d) at the partner level and would never be subject to section 163(j) at the partnership level.

A third approach would require a partnership to treat all of the interest expense from a trading activity as investment interest under section 163(d), regardless of whether any individual partners materially participate in the trading activity. Under this approach, the interest expense properly allocable to materially participating partners would never be subject to limitation under section 163(j), even though interest expense allocable to materially participating partners would also not be subject to limitation under section 163(d) at the individual partner level.

After considering the comments, Treasury Department and the IRS have concluded that the approach described in the preamble to the 2018 Proposed Regulations is inconsistent with the statutory language and intent of section 163(j)(5) because the second sentence of section 163(j)(5) specifically states that BIE shall not include investment interest expense. In addition, the Treasury Department and the IRS have determined that the second alternative approach, as described earlier, appears to be the most consistent with the intent of sections 163(d) and 163(j). Accordingly, these Proposed Regulations would interpret section 163(j)(5) as requiring a trading partnership to bifurcate its interest expense from a trading activity between partners that materially participate in the trading activity and partners that are passive investors, and as subjecting only the portion of the interest expense that is allocable to the materially participating partners to limitation under section 163(j) at the partnership level. The portion of interest expense from a trading activity allocable to passive investors will be subject to limitation under section 163(d) at the partner level, as provided in section 163(d)(5)(A)(ii).

In addition, these Proposed Regulations require that a trading partnership bifurcate all of its other items of income, gain, loss and deduction from its trading activity between partners that materially participate in the partnership's trading activity and partners that are passive investors. The portion of the partnership's other items of income, gain, loss or deduction from its trading activity properly allocable to the passive investors in the partnership will not be taken into account at the partnership level as items from a trade or business for purposes of applying section 163(j) at the partnership level. Instead, all such partnership items properly allocable to passive investors will be treated as items from an investment activity of the partnership, for purposes of sections 163(j) and 163(d).

This approach, in order to be effective, adopts the presumption that a trading partnership generally will possess knowledge regarding whether its individual partners are material participants in its trading activity. No rules currently exist requiring a partner to inform the partnership whether the partner has grouped activities of the partnership with other activities of the partner outside of the partnership. Therefore, the partnership might possess little or no knowledge regarding whether an individual partner has made such a grouping. Without this information, a trading partnership may presume that an individual partner is a passive investor in the partnership's trading activity based solely on the partnership's understanding as to the lack of work performed by the partner in that activity, whereas the partner may in fact be treated as a material participant in the partnership's trading activity by grouping that activity with one or more activities of the partner in which the partner materially participates. In order to avoid this result and the potential for abuse, a new rule is proposed for the section 469 activity grouping rules to provide that any activity described in section 163(d)(5)(A)(ii) may not be grouped with any other activity of the taxpayer, including any other activity described in section 163(d)(5)(A)(ii). The Treasury Department and the IRS invite comments regarding whether other approaches may be feasible and preferable to a special rule that prohibits the grouping of trading activities with other activities of a partner, such as adoption of a rule or reporting regime requiring all partners in the partnership to annually certify or report to the partnership whether they are material participants in a grouped activity that includes the partnership's trading activity.

The Treasury Department and the IRS further invite comments regarding whether similar rules should be adopted with respect to S corporations that may also be involved in trading activities, and whether such rules would be compatible with Subchapter S (for example, whether the bifurcation of items from the S corporation's trading activity between material participants and passive investors would run afoul of the second class of stock prohibition).

B. Fungibility of Publicly Traded Partnerships

In order to be freely marketable, each unit of a publicly traded partnership (PTP), as defined in § 1.7704–1, must have identical economic and tax characteristics so that such PTP units are fungible. For PTP units to be fungible, the section 704(b) capital account associated with each unit must be economically equivalent to the section 704(b) capital account of all other units of the same class, and a PTP unit buyer must receive equivalent tax allocations regardless of the specific unit purchased. In other words, from the perspective of a buyer, a PTP unit cannot have variable tax attributes depending on the identity of the PTP unit seller. In general, to achieve fungibility, a PTP (1) makes a section 754 election, pursuant to which a purchaser can insulate itself from its predecessor's allocable section 704(c) gain or loss through a section 743(b) basis adjustment, and (2) adopts the remedial allocation method under section 704(c) for all of its assets.

Pursuant to § 1.704–3(d)(1), a partnership adopts the section 704(c) remedial allocation method to eliminate distortions caused by the application of the ceiling rule, as defined in § 1.704–3(b)(1), under the section 704(c) traditional method. A partnership adopting the remedial allocation method eliminates ceiling rule distortions by creating remedial items and allocating those items to its partners. Under the remedial allocation method, a partnership first determines the amount of section 704(b) book items under § 1.704–3(d)(2) and the partners' section 704(b) distributive shares of such items. The partnership then allocates the corresponding tax items recognized by the partnership, if any, using the traditional method described in § 1.704–3(b)(1). If the ceiling rule causes the section 704(b) book allocation of an item to a noncontributing partner to differ from the tax allocation of the same item to the noncontributing partner, the partnership creates a remedial item of income, gain, loss, or deduction equal to the full amount of the difference and allocates it to the noncontributing partner. The partnership simultaneously creates an offsetting remedial item in an identical amount and allocates it to the contributing partner. In sum, by coupling the remedial allocation method with a section 754 election, PTP units remain fungible from a net tax perspective, regardless of the PTP unit seller's section 704(c) position.

However, even when the remedial allocation method is coupled with a section 754 election, the application of section 163(j) in the partnership context results in variable tax attributes for a buyer depending upon the tax characteristics of the interest held by the seller. The Treasury Department and the IRS have determined this is an inappropriate result for PTPs because PTPs, unlike other partnerships, always require that tax attributes be proportionate to economic attributes to retain the fungibility of their units. The Treasury Department and the IRS have determined that the manner in which section 163(j) applies in the partnership context should not result in the non-fungibility of PTP units. Accordingly, these Proposed Regulations provide a method, solely for PTPs, for applying section 163(j) in a manner that does not result in PTP units lacking fungibility.

Specifically, commenters identified three ways in which the 2018 Proposed Regulations may cause PTP units to be non-fungible. First, the method for allocating excess items may cause PTP units to be non-fungible. In general, under § 1.163(j)–6(f)(2), the allocation of the components of ATI dictate the allocation of a partnership's deductible BIE and section 163(j) excess items. Consequently, the unequal sharing of inside basis, including cost-recovery deductions, amortization, gain, and loss affects the ratio in which a partnership's section 163(j) excess items, as defined in § 1.163(j)–6(b)(6), are shared. A partner's share of section 163(j) excess items affects the tax treatment and economic consequences of the partner. For example, a greater share of excess taxable income enables a partner subject to section 163(j) to deduct more interest.

The Treasury Department and the IRS recognize that a non-pro rata sharing of inside basis could result in a non-pro rata allocation of excess items, which may result in PTP units lacking fungibility. Therefore, these Proposed Regulations would amend § 1.163(j)–6(f)(1)(iii) to provide that, solely for purposes of section 163(j), a PTP allocates section 163(j) excess items in accordance with the partners' shares of corresponding section 704(b) items that comprise ATI.

Second, the required adjustments to partner ATI for partner basis items (*e.g.,* section 743(b) income and loss) may cause PTP units to lack fungibility. A non-pro rata sharing of inside basis may result in a different allocation of partner basis items, as defined in § 1.163(j)–6(b)(2), and section 704(c) remedial items, as defined in § 1.163(j)–6(b)(3), among partners. Pursuant to § 1.163(j)–6(d)(2), partner basis items and remedial items are not taken into account in determining a partnership's ATI under § 1.163(j)–1(b)(1). Instead, partner basis items and section 704(c) remedial items affect the tax treatment and economic consequences of the partner. Similar to the disproportionate sharing of excess items discussed earlier, the disproportionate sharing of partner basis items and section 704(c) remedial items among partners may cause PTP units to lack fungibility.

The Treasury Department and the IRS recognize that a non-pro rata sharing of inside basis could result in different partner basis items and remedial items being allocated to different partners. Therefore, these Proposed Regulations would amend § 1.163(j)–6(e)(2)(ii) to provide that, solely for the purpose of determining remedial items under section 163(j), a PTP either allocates gain or loss that would otherwise be allocated under section 704(c) to a specific partner to all partners based on each partner's section 704(b) sharing ratio, or, for purposes of allocating cost recovery deductions under section 704(c), determines each partner's remedial items based on an allocation of the partnership's inside basis items among its partners in proportion to their share of corresponding section 704(b) items, rather than applying the traditional method as described in § 1.704–3(b).

Third, the treatment of section 704(c) remedial income allocations for taxable years beginning before 2022 may cause PTP units to lack fungibility. For taxable years beginning before January 1, 2022, when tentative taxable income is not reduced by depreciation and amortization deductions for purposes of determining ATI, a buyer acquiring PTP units with section 704(c) remedial income allocations (and an offsetting section 743(b) adjustment) will have an increase to its ATI that exceeds that of a buyer of the same number of otherwise fungible units that is not stepping into section 704(c) remedial income (with no corresponding section 743(b) deduction). While the net amount of the section 743(b) and section 704(c) remedial items is the same to both buyers, for taxable years beginning before January 1, 2022, different units would affect a buyer's ATI differently. The section 704(c) remedial income of a buyer of units with section 704(c) remedial income would be included in its ATI, while the section 743(b) deductions would not. Thus, a buyer of units with section 704(c) remedial income would increase its ATI each year (before 2022). A buyer of units with no section 704(c) remedial income, however, would add back any remedial depreciation and amortization deductions before 2022, and its ATI would be unaffected by the remedial deductions for such years.

The Treasury Department and the IRS recognize that, before 2022, a buyer of PTP units with inherent section 704(c) gain would include any remedial income and would not include section 743(b) deductions in its ATI. Therefore, these Proposed Regulations would amend § 1.163(j)–6(d)(2)(ii) to provide that, solely for purposes of section 163(j), a PTP treats the amount of any section 743(b) adjustment of a purchaser of a partnership unit that relates to a remedial item that the purchaser inherits from the seller as an offset to the related section 704(c) remedial item. The Treasury Department and the IRS request comments as to whether the approaches outlined adequately resolves the fungibility issues created by section 163(j).

C. Treatment of Business Interest Income and Business Interest Expense With Respect to Lending Transactions Between a Partnership and a Partner (Self-Charged Lending Transactions)

The 2018 Proposed Regulations reserved on the treatment of BII and BIE with respect to lending transactions between a partnership and a partner (self-charged lending transactions). The preamble to the 2018 Proposed Regulations requested comments regarding self-charged lending transactions. One commenter recommended the final regulations include rules under § 1.163(j)–6(n) akin to those contained in § 1.469–7 to identify self-charged interest income and expense and further allow such self-charged interest income and expense to be excluded from the definition of BIE and BII under section 163(j)(5) and (6), respectively. The same commenter recommended that the final regulations retain the rule in § 1.163(j)–3(b)(4), as set forth in the 2018 Proposed Regulations, which applies the section 163(j) limitation prior to the application of the passive activity loss rules of section 469. Other commenters recommended the Final Regulations exclude BIE and BII from the section 163(j) calculation where a partner or S-corporation shareholder lends to, or borrows from, a passthrough entity. These commenters recommended that the amount excluded be based on the amount of income or expense recognized by partners or shareholders that are lenders or borrowers, as well as partners or shareholders that are related to a lender or borrower partner within the meaning of section 267(b) because it would be appropriate to exclude the BII and BIE realized by the related parties for purposes of the section 163(j) calculation.

In response to these comments, the Treasury Department and the IRS propose adding a rule in proposed § 1.163(j)–6(n) to provide that, in the case of a lending transaction between a partner (lending partner) and partnership (borrowing partnership) in which the lending partner owns a direct interest (self-charged lending transaction), any BIE of the borrowing partnership attributable to the self-charged lending transaction is BIE of the borrowing partnership for purposes of § 1.163(j)–6. If in a given taxable year the lending partner is allocated EBIE from the borrowing partnership and has interest income attributable to the self-charged lending transaction (interest income), the lending partner shall treat such interest income as an allocation of excess business interest income (EBII) from the borrowing partnership in such taxable year, but only to the extent of the lending partner's allocation of EBIE from the borrowing partnership in such taxable year. To prevent the double counting of BII, the lending partner includes interest income that was re-characterized as EBII pursuant to proposed § 1.163(j)–6(n) only once when calculating the lending partner's own section 163(j) limitation. In cases where the lending partner is not a C corporation, to the extent that any interest income exceeds the lending partner's allocation of EBIE from the borrowing partnership for the taxable year, and such interest income otherwise would be properly treated as investment income of the lending partner for purposes of section 163(d) for that year, such excess amount of interest income will continue to be treated as investment income of the lending partner for that year for purposes of section 163(d).

The Treasury Department and the IRS generally agree that lending partners should not be adversely affected by the fact that, without special rules, the interest income received at the partner level from such lending transactions generally will be treated as investment income if the partner is not engaged in the trade or business of lending money, while the BIE of the partnership will be subject to section 163(j) and potentially limited at the partner level as EBIE. This situation would create a mismatch between the character of the interest income and of the interest expense at the partner level from the same lending transaction. These proposed rules would apply only to items of interest income attributable to the lending transaction and EBIE from the same partnership that arise in the same taxable year of the lending partner. By applying these proposed rules only to correct a mismatch in character that may occur at the partner level during a single taxable year, these proposed rules otherwise ensure that a partnership engaged in a self-charged lending transaction will be subject to the rules of section 163(j) to the same extent regardless of the sources of its loans.

These proposed rules will not apply in the case of an S corporation because BIE of an S corporation is carried over by the S corporation as a corporate-level attribute rather than immediately passed through to its shareholders. In the year such disallowed BIE is deductible at the corporate level, it is not separately stated, and it is not subject to further limitation under section 163(j) at either the S corporation or shareholder level. Therefore, a limited self-charged rule to ensure proper matching of the character of interest income and BIE at the shareholder level is not necessary. This approach is consistent with the treatment of S corporations as separate entities from their owners, both generally and specifically with respect to section 163(j).

However, the Treasury Department and the IRS recognize that issues analogous to the issues faced by partnerships in self-charged lending transactions exist with respect to lending transactions between S corporations and their shareholders. The Treasury Department and the IRS request comments on whether a similar rule is appropriate for S corporations in light of section 163(j)(4)(B) not applying and, if so, how such rule should be structured.

D. Partnership Basis Adjustments Upon Partner Dispositions

In general, a partnership's disallowed BIE is allocated to its partners as EBIE rather than carried forward at the partnership level in order to prevent the trafficking of deductions for BIE carryforwards in the partnership context. To achieve this, section 163(j)(4)(B)(iii)(I) provides that the adjusted basis of a partner in a partnership interest is reduced (but not below zero) by the amount of EBIE allocated to the partner. If a partner disposes of a partnership interest, section 163(j)(4)(B)(iii)(II) provides that the adjusted basis of the partner in the partnership interest is increased immediately before the disposition by the amount of any EBIE that was not treated as BIE paid or accrued by the partner prior to the disposition. Further, under section 163(j)(4)(B)(iii)(II), no deduction shall be allowed to the transferor or transferee for any EBIE resulting in a basis increase.

The Treasury Department and the IRS have determined that the basis increase required by section 163(j)(4)(B)(iii)(II) is not fully descriptive of what is occurring when a partner with EBIE disposes of its partnership interest. If EBIE is not treated as BIE paid or accrued by the partner pursuant to § 1.163(j)–6(g) prior to the partner disposing of its partnership interest (nondeductible EBIE), section 163(j)(4)(B)(iii)(II) treats such nondeductible EBIE as though it were a nondeductible expense of the partnership.

This nondeductible expense is not a nondeductible, non-capitalizable expense under section 705(a)(2)(B). If it were, the partner's basis in its partnership interest at the time of the disposition would already reflect such an expense. Instead, section 163(j)(4)(B)(iii)(II) requires the partner to increase its basis immediately before the disposition—in effect, treating the partner as though the partnership made a payment that decreased the value of the partnership interest but did not affect the partner's basis in its partnership interest. Thus, upon a disposition, section 163(j)(4) treats nondeductible EBIE as though it were a nondeductible, capitalizable expense of the partnership.

While the statute is clear that a partner increases the basis in its partnership interest immediately prior to a disposition by any nondeductible EBIE, it does not specifically state that there must also be a corresponding increase to the basis of partnership assets to account for the nondeductible, capitalized expense (*i.e.,* the nondeductible EBIE). The absence of a corresponding increase to the partnership's basis immediately before the partner's disposition would create distortions that are inconsistent with the intent of both section 163(j) and subchapter K of the Code.

For example, the basis increase attributable to nondeductible EBIE immediately before a liquidating distribution results in less gain recognized under section 731(a)(1) (or more loss recognized under section 731(a)(2)) for the partner disposing of its partnership interest. Consequently, following a liquidating distribution to a partner with EBIE, section 163(j)(4)(B)(iii)(II) causes a reduced section 734(b) adjustment if the partnership has a section 754 election in effect (versus the partner basis increase not occurring), resulting in basis disparity between the partnership's basis in its assets and the aggregate outside basis of the remaining partners.

To illustrate, consider the following example. In Year 1, A, B, and C formed partnership PRS by each contributing $1,000 cash. PRS borrowed $900, causing each partner's basis in PRS to increase by $300. Also in Year 1, PRS purchased Capital Asset X for $200. In Year 2, PRS pays $300 of BIE, all of which is disallowed and treated as EBIE. PRS allocated the $300 of EBIE to its partners, $100 each. Pursuant to § 1.163(j)–6(h)(2), each partner reduced its outside basis by its $100 allocation of EBIE to $1,200. In Year 3, when the fair market value of Capital Asset X is $3,200 and no partner's basis in PRS has changed, PRS distributed $1,900 to C in complete liquidation of C's partnership interest. PRS has a section 754 election in effect in Year 3.

Pursuant to § 1.163(j)–6(h)(3), C increases the adjusted basis of its partnership interest by $100 immediately before the disposition. Thus, C's section 731(a)(1) gain recognized on the disposition of its partnership interest is $900 (($1,900 cash + $300 relief of liabilities) − ($1,200 outside basis + $100 EBIE add-back)). Because the election under section 754 is in effect, PRS has a section 734(b) increase to the basis of its assets of $900 (the amount of section 731(a)(1) gain recognized by C). Under section 755, the entire adjustment is allocated to Capital Asset X. As a result, PRS's basis for Capital Asset X is $1,100 ($200 + $900 section 734(b) adjustment). Following the liquidation of C, PRS's basis in its assets ($1,500 of cash + $1,100 of Capital Asset X) does not equal the aggregate outside basis of partners A and B ($2,700).

The Treasury Department and the IRS have determined that basis disparity resulting from the absence of a corresponding inside basis increase, as described earlier, is an inappropriate result. Accordingly, these Proposed Regulations would provide for a corresponding inside basis increase that would serve as the partnership analog of section 163(j)(4)(B)(iii)(II). Specifically, proposed § 1.163(j)–6(h)(5) would provide that if a partner (transferor) disposes of its partnership interest, the partnership shall increase the adjusted basis of partnership property by an amount equal to the amount of the increase required under § 1.163(j)–6(h)(3), if any, to the adjusted basis of the partnership interest being disposed of by the transferor. Such increase in the adjusted basis of partnership property (§ 1.163(j)–6(h)(5) basis adjustment) shall be allocated among partnership properties in the same manner as a positive section 734(b) adjustment. Because a § 1.163(j)–6(h)(5) basis adjustment is taken into account when determining the gain or loss upon a sale of the asset, a § 1.163(j)–6(h)(5) basis adjustment prevents the shifting of built-in gain to the remaining partners.

These Proposed Regulations would adopt an approach that treats the increase in the adjusted basis of any partnership property resulting from a § 1.163(j)–6(h)(5) basis adjustment as not depreciable or amortizable under any section of the Code, regardless of whether the partnership property allocated such § 1.163(j)–6(h)(5) basis adjustment is otherwise generally depreciable or amortizable. This approach perceives EBIE as a deduction that was disallowed to the partnership (consistent with section 163(j)(4)(B)(iii)(II)), and thus should not result in a depreciable section 734(b) basis adjustment.

The Treasury Department and the IRS request comments on this approach. An alternative approach considered by the Treasury Department and the IRS would treat a § 1.163(j)–6(h)(5) basis adjustment as depreciable or amortizable if it is allocated to depreciable or amortizable property. However, section 163(j)(4)(B)(iii)(II) provides that no deduction shall be allowed to the transferor or transferee for any EBIE resulting in a basis increase to the partner that disposed of its interest. If a § 1.163(j)–6(h)(5) basis adjustment were depreciable or amortizable, a partnership—which can arguably be viewed as a transferee in a transaction in which a partner receives a distribution in complete liquidation of its partnership interest—could effectively deduct an expense that section 163(j)(4)(B)(iii)(II) states is permanently disallowed. The Treasury Department and the IRS request comments on whether treating a § 1.163(j)–6(h)(5) basis adjustment as potentially depreciable or amortizable is consistent with section 163(j)(4)(B)(iii)(II).

E. Treatment of Excess Business Interest Expense in Tiered Partnerships

1. Entity Approach

The preamble to the 2018 Proposed Regulations reserved and requested comments on the application of section 163(j)(4) to tiered partnership structures. Specifically, the preamble to the 2018 Proposed Regulations requested comments regarding whether, in a tiered partnership structure, EBIE should be allocated through an upper-tier partnership to the partners of upper-tier partnership. Additionally, comments were requested regarding how and when the basis of an upper-tier partnership partner should be adjusted when a lower-tier partnership has BIE that is limited under section 163(j).

In response, commenters recommended approaches that, in general, either (1) allocated EBIE through upper-tier partnership to the partners of upper-tier partnership (Aggregate Approach), or (2) did not allocate EBIE through upper-tier partnership to the partners of upper-tier partnership (Entity Approach). Commenters stated that both approaches reasonably implement Congressional intent of applying section 163(j) at the partnership level; however, the Entity

Approach reflects a stronger allegiance to entity treatment of partnerships for purposes of section 163(j). Commenters noted that the ultimate determination of which approach is more appropriate should rest, in large part, on whether partnerships or partners are more able to comply with the provision. The Entity Approach places more of that burden on partnerships, and the Aggregate Approach places more of the burden on partners. Commenters recommended that partnerships are better able to comply with an Entity Approach than partners are able to comply with an Aggregate Approach. Further, because the Entity Approach centers a significant portion of the compliance effort with partnerships, the Entity Approach may increase compliance and simplify Service review.

The Treasury Department and the IRS have concluded that an Entity Approach is the most consistent with the approach taken to partnerships under section 163(j)(4). Further, the Treasury Department and the IRS agree with commenters that partnerships are better able to comply with section 163(j) tiered partnership rules than partners. Accordingly, proposed § 1.163(j)–6(j)(3) would provide that if lower-tier partnership allocates excess business interest expense to upper-tier partnership, then upper-tier partnership reduces its basis in lower-tier partnership pursuant to § 1.163(j)–6(h)(2). Upper-tier partnership partners do not, however, reduce the bases of their upper-tier partnership interests pursuant to § 1.163(j)–6(h)(2) until upper-tier partnership treats such excess business interest expense as business interest expense paid or accrued pursuant to § 1.163(j)–6(g).

Although proposed § 1.163(j)–6(j)(3) would provide that EBIE allocated from a lower-tier partnership to an upper-tier partnership is not subject to further allocation by the upper-tier partnership, such EBIE necessarily reflects a reduction in the value of lower-tier partnership by the amount of the economic outlay that resulted in such EBIE. Accordingly, proposed § 1.163(j)–6(j)(2) would provide that if lower-tier partnership pays or accrues business interest expense and allocates such business interest expense to upper-tier partnership, then both upper-tier partnership and any direct or indirect partners of upper-tier partnership shall, solely for purposes of section 704(b) and the regulations thereunder, treat such business interest expense as a section 705(a)(2)(B) expenditure. Any section 704(b) capital account reduction resulting from such treatment occurs regardless of whether such business interest expense is characterized under this section as excess business interest expense or deductible business interest expense by lower-tier partnership. If upper-tier partnership subsequently treats any excess business interest expense allocated from lower-tier partnership as business interest expense paid or accrued pursuant to § 1.163(j)–6(g), the section 704(b) capital accounts of any direct or indirect partners of upper-tier partnership are not further reduced.

2. Basis and Carryforward Component of EBIE

Some commenters stated that an Entity Approach—that is, the approach these Proposed Regulations would adopt—would result in basis disparity between upper-tier partnership's basis in its assets and the aggregate basis of the upper-tier partners' interests in upper-tier partnership. The Treasury Department and the IRS do not agree. EBIE is neither an item of deduction nor a section 705(a)(2)(B) expense. If an allocation of EBIE from lower-tier partnership results in a reduction of the upper-tier partnership's basis in its lower-tier partnership interest, there is not a net reduction in the tax attributes of the upper-tier partnership. Rather, in such an event, upper-tier partnership merely exchanges one tax attribute (tax basis in its lower-tier partnership interest) for a different tax attribute (EBIE, which, in a subsequent year, could result in either a deduction or a basis adjustment). Thus, basis is preserved in this exchange.

Accordingly, proposed § 1.163(j)–6(j)(4) would provide that if lower-tier partnership allocates excess business interest expense to upper-tier partnership and such excess business interest expense is not suspended under section 704(d), then upper-tier partnership shall treat such excess business interest expense (UTP EBIE) as a nondepreciable capital asset, with a fair market value of zero and basis equal to the amount by which upper-tier partnership reduced its basis in lower-tier partnership pursuant to § 1.163(j)–6(h)(2) due to the allocation of such excess business interest expense. The fair market value of UTP EBIE, described in the preceding sentence, is not adjusted by any revaluations occurring under § 1.704–1(b)(2)(iv)(f).

In addition to generally treating UTP EBIE as having a basis component in excess of fair market value and, thus, built-in loss property, proposed § 1.163(j)–6(j)(4) would also provide that upper-tier partnership shall also treat UTP EBIE as having a carryforward component associated with it. The carryforward component of UTP EBIE shall equal the amount of excess business interest expense allocated from lower-tier partnership to upper-tier partnership under § 1.163(j)–6(f)(2) that is treated as such under § 1.163(j)–6(h)(2) by upper-tier partnership.

The carryforward component of UTP EBIE and the basis component of such UTP EBIE will always be equal immediately following the allocation of such EBIE from lower-tier partnership to upper-tier partnership if, at the time of such allocation, upper-tier partnership was required to reduce its section 704(b) capital account pursuant to proposed § 1.163(j)–6(j)(2) due to such allocation. However, subsequent to such initial allocation of EBIE from lower-tier partnership to upper-tier partnership, disparities between the carryforward component of UTP EBIE and the basis component of such UTP EBIE may arise as a result of proposed § 1.163(j)–6(j)(7).

Similar to the treatment of partner basis items (which do not affect the ATI of a partnership), proposed § 1.163(j)–6(j)(7)(i) would provide that negative basis adjustments under sections 734(b) and 743(b) allocated to UTP EBIE do not affect the carryforward component of such UTP EBIE; rather, negative basis adjustments under sections 734(b) and 743(b) affect only the basis component of such UTP EBIE. Although section 734(b) adjustments do affect a partnership's computation of ATI, the Treasury Department and the IRS have determined that negative section 734(b) adjustments, if allocated to UTP EBIE, should not reduce the carryforward component of such UTP EBIE. The purpose of proposed § 1.163(j)–6(j)(7)—in addition to preventing the duplication of loss—is to make partners indifferent for section 163(j) purposes as to whether a partner exiting upper-tier partnership sells its interest or receives a liquidating distribution from upper-tier partnership. Excluding negative section 734(b) adjustments from proposed § 1.163(j)–6(j)(7) would frustrate this purpose.

3. UTP EBIE Conversion Events

Proposed § 1.163(j)–6(j)(4) would further provide that if an allocation of excess business interest expense from lower-tier partnership is treated as UTP EBIE of upper-tier partnership, upper-tier partnership shall treat such allocation of excess business interest expense from lower-tier partnership as UTP EBIE until the occurrence of an UTP EBIE conversion event described in proposed § 1.163(j)–6(j)(5). In the non-tiered context, EBIE generally has two types of conversion events. The first EBIE conversion event is when EBIE is treated as BIE paid or accrued pursuant to § 1.163(j)–6(g). The second EBIE conversion event is the basis addback that occurs pursuant to proposed § 1.163(j)–6(h)(3) when a partner disposes of its interest in a partnership. Proposed § 1.163(j)–6(j)(5)(i) and (ii), respectively, would provide guidance regarding these two types of conversion events in the tiered partnership context.

a. First Type of Conversion Event—UTP EBIE Treated as Paid or Accrued

Regarding the first type of conversion event, proposed § 1.163(j)–6(j)(5)(i) would provide that to the extent upper-tier partnership is allocated excess taxable income (or excess business interest income) from lower-tier partnership, or § 1.163(j)–6 (m)(3) applies, upper-tier partnership shall apply proposed § 1.163(j)–6(j)(5)(i)(A) through (C).

First, proposed § 1.163(j)–6(j)(5)(i)(A) requires upper-tier partnership to apply the rules in § 1.163(j)–6(g) to its UTP EBIE, using any reasonable method (including, for example, FIFO and LIFO) to determine which UTP EBIE is treated as business interest expense paid or accrued pursuant § 1.163(j)–6(g). If § 1.163(j)–6(m)(3) applies, upper-tier partnership shall treat all of its UTP EBIE from lower-tier partnership as paid or accrued.

Proposed § 1.163(j)–6(j)(5)(i)(A) would provide that upper-tier partnership must determine which of its UTP EBIE is treated as paid or accrued, as opposed to just providing that upper-tier partnership reduces its UTP EBIE, because UTP EBIE is not necessarily a unified tax attribute of upper-tier partnership. UTP EBIE of upper-tier partnership could have been allocated in different years, have different bases, and have different specified partners (defined in the next paragraph). For example, assume $30 of UTP EBIE was allocated a negative $10 section 734(b) adjustment, resulting in the aggregate of upper-tier partnership's UTP EBIE having a carryforward component of $30 and basis component of $20. Thus, such UTP EBIE could, at most, result in $20 of deduction (the basis of such UTP EBIE). However, upper-tier partnership does not necessarily need $100 of ETI (or $30 of EBII) to deduct such $20. Rather, if upper-tier partnership was allocated $20 of EBII, upper-tier partnership could deduct $20 of business interest expense if, using a reasonable method, it determined the $20 of UTP EBIE with full basis was the UTP EBIE treated as business interest expense paid or accrued pursuant to § 1.163(j)–6(j)(5)(i)(A). Following such treatment, upper-tier partnership would still have $10 of UTP EBIE with $0 basis remaining (that is, $10 of carryforward component and $0 of basis component).

Second, with respect to any UTP EBIE treated as business interest expense paid or accrued in proposed § 1.163(j)–6(j)(5)(i)(A), proposed § 1.163(j)–6(j)(5)(i)(B) would require upper-tier partnership to allocate any business interest expense that was formerly such UTP EBIE to its specified partner. For purposes of proposed § 1.163(j)–6(j), the term specified partner refers to the partner of upper-tier partnership that, due to the initial allocation of excess business interest expense from lower-tier partnership to upper-tier partnership, was required to reduce its section 704(b) capital account pursuant to proposed § 1.163(j)–6(j)(2). Similar principles apply if the specified partner of such business interest expense is itself a partnership.

Proposed § 1.163(j)–6(j)(6) would provide rules if a specified partner disposes of its interest. Specifically, proposed § 1.163(j)–6(j)(6)(i) would provide that if a specified partner (transferor) disposes of an upper-tier partnership interest (or an interest in a partnership that itself is a specified partner), the portion of any UTP EBIE to which the transferor's status as specified partner relates is not reduced pursuant to proposed § 1.163(j)–6(j)(5)(ii). Stated otherwise, if a partner of an upper-tier partnership disposes of its interest in the upper-tier partnership, an interest in the lower-tier partnership held by upper-tier partnership is not deemed to have been similarly disposed of for purposes of proposed § 1.163(j)–6(j)(5)(ii). See Rev. Rul. 87–115. Rather, such UTP EBIE attributable to the interest disposed of is retained by upper-tier partnership and the transferee is treated as the specified partner for purposes of proposed § 1.163(j)–6(j) with respect to such UTP EBIE. Thus, upper-tier partnership must allocate any business interest expense that was formerly such UTP EBIE to the transferee.

Additionally, proposed § 1.163(j)–6(j)(6)(ii) would provide special rules regarding the specified partner of UTP EBIE following certain nonrecognition transactions. Proposed § 1.163(j)–6(j)(6)(ii)(A) would provide that if a specified partner receives a distribution of property in complete liquidation of an upper-tier partnership interest, the portion of UTP EBIE of upper-tier partnership attributable to the liquidated interest shall not have a specified partner. If a specified partner (transferee) receives a distribution of an interest in upper-tier partnership in complete liquidation of a partnership interest, the transferee is the specified partner with respect to UTP EBIE of upper-tier partnership only to the same extent it was prior to the distribution. Similar principles apply where an interest in a partnership that is a specified partner is distributed in complete liquidation of a transferee's partnership interest.

Proposed § 1.163(j)–6(j)(6)(ii)(B) would further provide that if a specified partner (transferor) contributes an upper-tier partnership interest to a partnership (transferee), the transferee is treated as the specified partner for purposes of proposed § 1.163(j)–6(j) with respect to the portion of the UTP EBIE attributable to the contributed interest. Following the transaction, the transferor continues to be the specified partner with respect to the UTP EBIE attributable to the contributed interest. Similar principles apply where an interest in a partnership that is a specified partner is contributed to a partnership.

Finally, after determining the specified partner of the UTP EBIE treated as business interest expense paid or accrued in proposed § 1.163(j)–6(j)(5)(i)(A) and allocating such business interest expense to its specified partner pursuant to proposed § 1.163(j)–6(j)(5)(i)(B), proposed § 1.163(j)–6(j)(5)(i)(C) would require upper-tier partnership to, in the manner provided in proposed § 1.163(j)–6(j)(7)(ii) (or (iii), as the case may be), take into account any negative basis adjustments under section 734(b) previously made to the UTP EBIE treated as business interest expense paid or accrued in (A) earlier. Additionally, persons treated as specified partners with respect to the UTP EBIE treated as business interest expense paid or accrued in (A) earlier shall take any negative basis adjustments under section 743(b) into account in the manner provided in proposed § 1.163(j)–6(j)(7)(ii) (or (iii), as the case may be).

Proposed § 1.163(j)–6(j)(7)(ii) would provide that if UTP EBIE that was allocated a negative section 734(b) adjustment is subsequently treated as deductible business interest expense, then such deductible business interest expense does not result in a deduction to the upper-tier partnership or the specified partner of such deductible business interest expense. If UTP EBIE that was allocated a negative section 743(b) adjustment is subsequently treated as deductible business interest expense, the specified partner of such deductible business interest expense recovers any negative section 743(b) adjustment attributable to such deductible business interest expense (effectively eliminating any deduction for such deductible business interest expense).

Proposed § 1.163(j)–6(j)(7)(iii) would provide that if UTP EBIE that was allocated a negative section 734(b) or 743(b) adjustment is subsequently treated as excess business interest expense, the specified partner's basis decrease in its upper-tier partnership interest required under proposed § 1.163(j)–6(h)(2) is reduced by the amount of the negative section 734(b) or 743(b) adjustment previously made to such excess business interest expense. If such excess business interest expense is subsequently treated as business interest expense paid or accrued by the specified partner, no deduction shall be allowed for any of such business interest expense. If the specified partner of such excess business interest expense is a partnership, such excess business interest expense is considered UTP EBIE that was previously allocated a negative section 734(b) adjustment for purposes of proposed § 1.163(j)–6(j).

b. Second Type of Conversion Event—UTP EBIE Reduction

Regarding the second type of conversion event, proposed § 1.163(j)–6(j)(5)(ii) would provide that if upper-tier partnership disposes of a lower-tier partnership interest (transferred interest), upper-tier partnership shall apply proposed § 1.163(j)–6(j)(5)(ii)(A) through (C).

First, proposed § 1.163(j)–6(j)(5)(ii)(A) would require upper-tier partnership to apply the rules in § 1.163(j)–6(h)(3) (except as provided in (B) and (C) later), using any reasonable method (including, for example, FIFO and LIFO) to determine which UTP EBIE is reduced pursuant to § 1.163(j)–6(h)(3). Stated otherwise, proposed § 1.163(j)–6(j)(5)(ii)(A) would require upper-tier partnership to apply all of the rules in § 1.163(j)–6(h)(3), except for the rule that determines the amount of the basis increase immediately before the disposition to the disposed of interest (the first sentence of § 1.163(j)–6(h)(3)). In lieu of applying the first sentence of § 1.163(j)–6(h)(3), upper-tier partnership would apply proposed § 1.163(j)–6(j)(5)(ii)(B) and (C) to determine the amount of such basis increase.

Second, proposed § 1.163(j)–6(j)(5)(ii)(B) would require upper-tier partnership to increase the adjusted basis of the transferred interest immediately before the disposition by the total amount of the UTP EBIE that was reduced in (A) earlier (the amount of UTP EBIE proportionate to the transferred interest). For example, if upper-tier partnership disposed of half of its lower-tier partnership interest while it held $40 of UTP EBIE allocated from lower tier partnership, upper-tier partnership would increase the adjusted basis of the disposed of lower-tier partnership interest by $20. However, immediately before the disposition, such $20 increase may be reduced pursuant to proposed § 1.163(j)–6(j)(5)(ii)(C).

Third, proposed § 1.163(j)–6(j)(5)(ii)(C) would require upper-tier partnership to, in the manner provided in proposed § 1.163(j)–6(j)(7)(iv), take into account any negative basis adjustments under sections 734(b) and 743(b) previously made to the UTP EBIE that was reduced in (A) earlier. Proposed § 1.163(j)–6(j)(7)(iv) would provide that if UTP EBIE that was allocated a negative section 734(b) or 743(b) adjustment is reduced pursuant to proposed § 1.163(j)–6(j)(5)(ii)(A), the amount of upper-tier partnership's basis increase under proposed § 1.163(j)–6(j)(5)(ii)(B) to the disposed of lower-tier partnership interest is reduced by the amount of the negative section 734(b) or 743(b) adjustment previously made to such UTP EBIE.

Continuing with the previous example, assume that $5 of the $20 of UTP EBIE reduced pursuant to proposed § 1.163(j)–6(j)(5)(ii)(A) was previously allocated a $5 negative section 743(b) adjustment. Pursuant to proposed § 1.163(j)–6(j)(5)(ii)(C), upper-tier partnership would reduce the $20 increase it determined under proposed § 1.163(j)–6(j)(5)(ii)(B) by $5. Thus, the adjusted basis of the lower-tier partnership interest being disposed of would be increased by $15 immediately before the disposition. Consequently, lower-tier partnership would have a corresponding § 1.163(j)–6(h)(5) basis adjustment to its property of $15.

4. Anti-Loss Trafficking Rules

Proposed § 1.163(j)–6(j) generally relies on negative sections 734(b) and 743(b) adjustments to prevent a partner from deducting business interest expense that was formerly UTP EBIE if such partner did not bear the economic cost of such business interest expense payment. To the extent a negative section 734(b) or 743(b) adjustment fails to prohibit such a deduction (or basis increase under proposed § 1.163(j)–6(j)(5)(ii)), the anti-loss trafficking rules in proposed § 1.163(j)–6(j)(8) would prohibit such a deduction (or basis addback under proposed § 1.163(j)–6(j)(5)(ii)).

The anti-loss trafficking rule under proposed § 1.163(j)–6(j)(8)(i) would prohibit the trafficking of business interest expense by providing that no deduction shall be allowed to any transferee specified partner for any business interest expense derived from a transferor's share of UTP EBIE. For purposes of proposed § 1.163(j)–6(j), the term transferee specified partner refers to any specified partner that did not reduce its section 704(b) capital account upon the initial allocation of excess business interest expense from lower-tier partnership to upper-tier partnership pursuant to proposed § 1.163(j)–6(j)(2). However, the transferee described in proposed § 1.163(j)–6(j)(ii)(B) is not a transferee specified partner for purposes of proposed § 1.163(j)–6(j).

Proposed § 1.163(j)–6(j)(8)(i) would also provide the mechanism for disallowing such BIE. Proposed § 1.163(j)–6(j)(8)(i) would provide that if, pursuant to proposed § 1.163(j)–6(j)(5)(i)(B), a transferee specified partner is allocated business interest expense derived from a transferor's share of UTP EBIE (business interest expense to which the partner's status as transferee specified partner relates), the transferee specified partner is deemed to recover a negative section 743(b) adjustment with respect to, and in the amount of, such business interest expense and takes such negative section 743(b) adjustment into account in the manner provided in proposed § 1.163(j)–6(j)(7)(ii) (or (iii), as the case may be), regardless of whether a section 754 election was in effect or a substantial built-in loss existed at the time of the transfer by which the transferee specified partner acquired the transferred interest. However, to the extent a negative section 734(b) or 743(b) adjustment was previously made to such business interest expense, the transferee specified partner does not recover an additional negative section 743(b) adjustment pursuant to this paragraph.

Additionally, the anti-loss trafficking rule under proposed § 1.163(j)–6(j)(8)(ii) would prohibit the trafficking of BIE that was formerly the UTP EBIE of a specified partner that received a distribution in complete liquidation of its upper-tier partnership interest. Specifically, proposed § 1.163(j)–6(j)(8)(ii) would provide that if UTP EBIE does not have a specified partner (as the result of a transaction described in proposed § 1.163(j)–6(j)(6)(ii)(A)), upper-tier partnership shall not allocate any business interest expense that was formerly such UTP EBIE to its partners. Rather, for purposes of applying § 1.163(j)–6(f)(2), upper-tier partnership shall treat such business interest expense as the allocable business interest expense (as defined in

§ 1.163(j)–6(f)(2)(ii)) of a § 1.163(j)–6(j)(8)(ii) account.

Any deductible business interest expense and excess business interest expense allocated to a § 1.163(j)–6(j)(8)(ii) account at the conclusion of the eleven-step computation set forth in § 1.163(j)–6(f)(2) is not tracked in future years. Treating such business interest expense as the allocable business interest expense of a separate account for purposes of applying § 1.163(j)–6(f)(2)(ii) ensures that partners of upper-tier partnership do not support a deduction for such business interest expense (for which no deduction will be allowed) using their shares of allocable ATI and allocable business interest income before supporting a deduction for their own shares of allocable business interest expense (for which a deduction may be allowed).

Additionally, if UTP EBIE that does not have a specified partner (as the result of a transaction described in proposed § 1.163(j)–6(j)(6)(ii)(A)) is treated as paid or accrued pursuant to § 1.163(j)–6(g), upper-tier partnership shall make a § 1.163(j)–6(h)(5) basis adjustment to its property in the amount of the adjusted basis (if any) of such UTP EBIE at the time such UTP EBIE is treated as business interest expense paid or accrued pursuant to § 1.163(j)–6(g). The purpose of this § 1.163(j)–6(h)(5) basis adjustment is to preserve basis in the system.

Thus, any time upper-tier partnership treats UTP EBIE as business interest expense paid or accrued pursuant to proposed § 1.163(j)–6(j)(5)(i)(A) it must apply proposed § 1.163(j)–6(j)(8)(i) and (ii). In application, upper-tier partnership would generally undertake the following analysis when applying proposed § 1.163(j)–6(j)(8)(i) and (ii). With respect to any UTP EBIE treated as business interest expense paid or accrued pursuant to proposed § 1.163(j)–6(j)(5)(i)(A) (UTP BIE), upper-tier partnership must first determine whether such UTP BIE has a specified partner. If it does not have a specified partner, upper-tier partnership must apply proposed § 1.163(j)–6(j)(8)(ii), which, in general, requires upper-tier partnership to capitalize the basis (if any) of such UTP BIE into the basis of upper-tier partnership property via a § 1.163(j)–6(h)(5) basis adjustment.

If UTP BIE does have a specified partner, upper-tier partnership must next determine whether the specified partner of such UTP BIE reduced its section 704(b) capital account upon the initial allocation of such excess business interest expense from lower-tier partnership to upper-tier partnership pursuant to proposed § 1.163(j)–6(j)(2). If the specified partner did reduce its section 704(b) capital account upon such initial allocation, then any deduction for such UTP BIE is not disallowed under proposed § 1.163(j)–6(j)(8)(i). However, if the specified partner did not reduce its section 704(b) capital account upon such initial allocation, upper-tier partnership must next determine whether such specified partner is a transferee described in proposed § 1.163(j)–6(j)(6)(ii)(B). If it is, then any deduction for such UTP BIE is not disallowed under proposed § 1.163(j)–6(j)(8)(i). However, if the specified partner is not a transferee described in proposed § 1.163(j)–6(j)(6)(ii)(B), then it is a transferee specified partner, as defined in proposed § 1.163(j)–6(j)(8)(i). As a result, any deduction for such UTP BIE is disallowed under proposed § 1.163(j)–6(j)(8)(i). If there are multiple tiers of partnerships, each tier must apply these rules.

Finally, proposed § 1.163(j)–6(j)(8)(iii) would provide a similar mechanism to proposed § 1.163(j)–6(j)(8)(i) for disallowing basis addbacks under § 1.163(j)–6(h)(3) for certain UTP EBIE. Specifically, proposed § 1.163(j)–6(j)(8)(iii) would provide that no basis increase under proposed § 1.163(j)–6(j)(5)(ii) shall be allowed to upper-tier partnership for any disallowed UTP EBIE. For purposes of § 1.163(j)–6, the term disallowed UTP EBIE refers to any UTP EBIE that has a specified partner that is a transferee specified partner (as defined in proposed § 1.163(j)–6(j)(8)(i)) and any UTP EBIE that does not have a specified partner (as the result of a transaction described in proposed § 1.163(j)–6(j)(6)(ii)(A)). For purposes of applying proposed § 1.163(j)–6(j)(5)(ii), upper-tier partnership shall treat any disallowed UTP EBIE in the same manner as UTP EBIE that has previously been allocated a negative section 734(b) adjustment. However, upper-tier partnership does not treat disallowed UTP EBIE as though it were allocated a negative section 734(b) adjustment pursuant to this paragraph to the extent a negative section 734(b) or 743(b) adjustment was previously made to such disallowed UTP EBIE.

5. Foundational Determinations

In general, the rules under proposed § 1.163(j)–6(j) are derived from the following three foundational determinations made by the Treasury Department and the IRS. First, basis is preserved when upper-tier partnership exchanges basis in its lower-tier partnership for EBIE allocated from lower-tier partnership (UTP EBIE). Thus, upper-tier partnership generally must treat UTP EBIE in the same manner as built-in loss property. Second, UTP EBIE has two components—a basis component and a carryforward component. In general, negative basis adjustments under section 734(b) and 743(b) reduce the basis component of UTP EBIE (and thus, any possible deduction for UTP EBIE), but do not reduce the carryforward component of UTP EBIE; only the two conversion events in proposed § 1.163(j)–6(j)(5) are capable of reducing the carryforward component of UTP EBIE. Third, upper-tier partnership must allocate any business interest expense that was formerly UTP EBIE to its specified partner—that is, the partner that reduced its section 704(b) capital account at the time of the initial allocation of the UTP EBIE from lower-tier partnership to upper-tier partnership. If there is a transfer of a partnership interest, the transferor generally steps into the shoes of the transferee's status as specified partner, but may not deduct any business interest expense derived from the transferor's share of UTP EBIE.

The Treasury Department and the IRS request comments on this approach. Specifically, the Treasury Department and the IRS request comments on whether further guidance on the treatment of UTP EBIE under the rules of subchapter K of the Code is necessary.

F. Partner Basis Adjustments Upon a Distribution

Under the 2018 Proposed Regulations, if a partner disposed of all or substantially all of its partnership interest, the adjusted basis of the partnership interest was increased immediately before the disposition by the entire amount of the EBIE not previously treated as paid or accrued by the partner. If a partner disposed of less than substantially all of its interest in a partnership, the partner could not increase its basis by any portion of the EBIE not previously treated as paid or accrued by the partner. The Treasury Department and the IRS requested comments on this approach in the preamble to the 2018 Proposed Regulations.

As discussed in the preamble to Final Regulations, commenters cited multiple concerns with the approach adopted in the 2018 Proposed Regulations and recommended that the Final Regulations adopt a proportionate approach. Under such an approach, a partial disposition of a partnership interest would trigger a proportionate EBIE basis addback and corresponding decrease in such partner's EBIE carryover. The Treasury

Department and the IRS agreed with commenters. Accordingly, § 1.163(j)–6(h)(3) provides for a proportionate approach.

In general, a distribution from a partnership is either a current distribution or a liquidating distribution; the concept of a redemptive distribution does not exist in the partnership context. Accordingly, proposed § 1.163(j)–6(h)(4) would provide that, for purposes of § 1.163(j)–6(h)(3), a disposition includes a distribution of money or other property by the partnership to a partner in complete liquidation of the partner's interest in the partnership. Proposed § 1.163(j)–6(h)(4) would further provide that, for purposes of § 1.163(j)–6(h)(3), a current distribution of money or other property by the partnership to a continuing partner is not a disposition for purposes of § 1.163(j)–6(h)(3). The Treasury Department and the IRS request comments on whether a current distribution of money or other property by the partnership to a continuing partner as consideration for an interest in the partnership should also trigger an addback and, if so, how to determine the appropriate amount of the addback.

G. Allocable ATI and Allocable Business Interest Income of Upper-Tier Partnership Partners

Section 1.163(j)–6(f)(2) provides an eleven-step computation necessary for properly allocating a partnership's deductible BIE and section 163(j) excess items among its partners. Pursuant to § 1.163(j)–6(f)(2)(ii), a partnership must determine each of its partner's allocable share of each section 163(j) item under section 704(b) and the regulations under section 704 of the Code, including any allocations under section 704(c), other than remedial items. Further, § 1.163(j)–6(f)(2)(ii) provides that the term allocable ATI means a partner's distributive share of the partnership's ATI (that is, a partner's distributive share of gross income and gain items comprising ATI less such partner's distributive share of gross loss and deduction items comprising ATI), and the term allocable business interest income means a partner's distributive share of the partnership's business interest income.

In general, if a partnership is not a partner in a partnership, each dollar of taxable income that is properly allocable to a trade or business will have a corresponding dollar of ATI associated with it. Accordingly, in the non-tiered partnership context, if a partner's share of gross income and gain items comprising ATI less such partner's share of gross loss and deduction items comprising ATI equals $1, such partner will have $1 of allocable ATI for purposes of § 1.163(j)–6(f)(2)(ii).

However, if a partnership is a partner in a partnership, each dollar of taxable income that is properly allocable to a trade or business may not have a full dollar of ATI associated with it. Section 163(j)(4)(A)(ii)(I) provides that the ATI of a partner in a partnership is determined without regard to such partner's distributive share of any items of income, gain, deduction, or loss of such partnership. Further, section 163(j)(4)(A)(ii)(II) provides that a partner only increases its ATI by its distributive share of a partnership's ETI.

To illustrate, consider the following example. LTP has $100 of income and $100 of loss properly allocable to a trade or business. Thus, LTP has $0 of ATI. LTP specially allocates the $100 of income to partner UTP. Under section 163(j)(4)(A)(ii)(I), UTP does not treat such $100 of income as ATI. Additionally, UTP has $300 of income properly allocable to a trade or business, which UTP properly treats as ATI. Here, UTP's taxable income that is properly allocable to a trade or business ($400) does not equal the amount of its ATI ($300).

The Treasury Department and the IRS recognize that a special rule is necessary to coordinate situations like the one illustrated earlier with the general requirement under § 1.163(j)–6(f)(2)(ii) for partnerships to determine a partner's allocable ATI based on such partner's allocation of items comprising the ATI of the partnership. Accordingly, proposed § 1.163(j)–6(j)(9) would provide that, when applying § 1.163(j)–6(f)(2)(ii), an upper-tier partnership determines the allocable ATI and allocable business interest income of each of its partners in the manner provided in proposed § 1.163(j)–6(j)(9). Specifically, if an upper-tier partnership's net amount of tax items that comprise (or have ever comprised) ATI is greater than or equal to its ATI, upper-tier partnership applies the rules in paragraph (j)(9)(ii)(A) to determine each partner's allocable ATI. However, if an upper-tier partnership's net amount of tax items that comprise (or have ever comprised) ATI is less than its ATI, upper-tier partnership applies the rules in proposed § 1.163(j)–6(j)(9)(ii)(B) to determine each partner's allocable ATI. To determine each partner's allocable business interest income, an upper-tier partnership applies the rules in proposed § 1.163(j)–6(j)(9)(iii).

H. Qualified Expenditures

The 2018 Proposed Regulations provided that partnership ATI is reduced by deductions claimed under sections 173 (relating to circulation expenditures), 174(a) (relating to research and experimental expenditures), 263(c) (relating to intangible drilling and development expenditures), 616(a) (relating to mine development expenditures), and 617(a) (relating to mining exploration expenditures) (collectively ''qualified expenditures''). As a result, deductions for qualified expenditures reduced the amount of business interest expense a partnership could potentially deduct.

A partner may elect to capitalize its distributive share of any qualified expenditures of a partnership under section 59(e)(4)(C) or may be required to capitalize a portion of its distributive share of certain qualified expenditures of a partnership under section 291(b). As a result, the taxable income reported by a partner in a taxable year attributable to the ownership of a partnership interest may exceed the amount of taxable income reported to the partner on a Schedule K–1.

Commenters on the 2018 Proposed Regulations recommended that a distributive share of partnership deductions capitalized by a partner under section 59(e) or section 291(b) increase the ATI of the partner because qualified expenditures reduce both partnership ATI and excess taxable income, but may not reduce the taxable income of a partner. Two different approaches for achieving this result were suggested: (1) Adjust the excess taxable income of the partnership, resulting in an increase to partner ATI, and (2) increase the ATI of the partner directly, without making any adjustments to partnership excess taxable income.

The Treasury Department and IRS agree that a distributive share of partnership deductions capitalized by a partner under section 59(e) should increase the ATI of the partner and adopt the recommended approach of increasing the ATI of the partner directly, without making any adjustments to partnership excess taxable income. The approach of increasing partner ATI by adjusting partnership excess taxable income is rejected, as it would result in partnerships with more excess taxable income than ATI—a result not possible under the current statutory conceptual framework. The Treasury Department and IRS have the authority to adjust ATI, but do not have a similar grant of authority to make adjustments to partnership excess taxable income, which is explicitly defined by statute.

Accordingly, proposed § 1.163(j)–6(e)(6) would provide that the ATI of a partner is increased by the portion of such partner's allocable share of qualified expenditures (as defined in section 59(e)(2)) to which an election under section 59(e) applies. Any deduction allowed under section 59(e)(1) would be taken into account in determining a partner's ATI pursuant to § 1.163(j)–1(b). Proposed § 1.163(j)–6(l)(4)(iv) would provide a similar rule in the S corporation context.

The Treasury Department and IRS are aware that a similar issue exists in the context of depletion and request comments as to whether a similar partner level add-back is appropriate. The Treasury Department and IRS are also aware that a partner may be required to capitalize certain qualified expenditures of a partnership under section 291(b) and request comments as to whether a similar partner level add-back is appropriate.

I. CARES Act Partnership Rules

As stated in the Background section of this preamble, section 163(j)(10), as enacted by the CARES Act, provides special rules for partners and partnerships for taxable years beginning in 2019 or 2020. Under sections 163(j)(10)(A)(i) and 163(j)(10)(A)(ii)(I), for partnerships, the amount of business interest that may be deductible under section 163(j)(1) for taxable years beginning in 2020 is computed using the 50 percent ATI limitation. The 50 percent ATI limitation does not apply to partnerships for taxable years beginning in 2019. See section 163(j)(10)(A)(ii)(I). Under section 163(j)(10)(A)(iii), a partnership may elect to not apply the 50 percent ATI limitation and, instead, to apply the 30 percent ATI limitation. This election is made by the partnership.

Under section 163(j)(10)(A)(ii)(II), a partner treats 50 percent of its allocable share of a partnership's excess business interest expense for 2019 as a business interest expense in the partner's first taxable year beginning in 2020 that is not subject to the section 163(j) limitation (50 percent EBIE rule). The remaining 50 percent of the partner's allocable share of the partnership's 2019 excess business interest expense remains subject to the section 163(j) limitation applicable to excess business interest expense carried forward at the partner level. A partner may elect out of the 50 percent EBIE rule. Proposed § 1.163(j)–6(g)(4) provides further guidance on the 50 percent EBIE rule.

Additionally, section 163(j)(10)(B)(i) allows a taxpayer to elect to substitute its 2019 ATI for the taxpayer's 2020 ATI in determining the taxpayer's section 163(j) limitation for any taxable year beginning in 2020. Section 1.163(j)–2(b)(3) and (4) of the Final Regulations provide general rules regarding this election. Proposed § 1.163(j)–6(d)(5) provides further guidance on this election in the partnership context. The Treasury Department and the IRS request comments on these proposed rules and on whether further guidance is necessary.

V. Proposed § 1.163(j)–7: Application of the Section 163(j) Limitation to Foreign Corporations and United States Shareholders

Proposed § 1.163(j)–7 in these Proposed Regulations (Proposed § 1.163(j)–7) provides general rules regarding the application of the section 163(j) limitation to foreign corporations and U.S. shareholders of CFCs. This section V describes proposed § 1.163(j)–7 contained in the 2018 Proposed Regulations, the comments received on proposed § 1.163(j)–7 contained in the 2018 Proposed Regulations, and Proposed § 1.163(j)–7.

A. Overview of Proposed § 1.163(j)–7 Contained in the 2018 Proposed Regulations

1. General Application of Section 163(j) Limitation to Applicable CFCs

The 2018 Proposed Regulations clarify that, consistent with § 1.952–2, section 163(j) and the section 163(j) regulations apply to determine the deductibility of an applicable CFC's BIE in the same manner as these provisions apply to determine the deductibility of a domestic C corporation's BIE. The 2018 Proposed Regulations define an applicable CFC as a CFC in which at least one U.S. shareholder owns stock within the meaning of section 958(a). However, in certain cases, the 2018 Proposed Regulations allow certain applicable CFCs to make a CFC group election and be treated as part of a CFC group for purposes of computing the applicable CFC's section 163(j) limitation.

2. Limitation on Amount of Business Interest Expense of a CFC Group Member Subject to the Section 163(j) Limitation

Under the 2018 Proposed Regulations, if a CFC group election is in effect, the amount of BIE of a CFC group member that is subject to the section 163(j) limitation is limited to the amount of the CFC group member's allocable share of the CFC group's applicable net BIE (which is equal to the sum of the BIE of all CFC group members, reduced by the BII of all CFC group members). Thus, for example, if a CFC group has no debt other than loans between CFC group members, no portion of the BIE of a CFC group member would be subject to the section 163(j) limitation. A CFC group member's allocable share is computed by multiplying the applicable net BIE of the CFC group by a fraction, the numerator of which is the CFC group member's net BIE (computed on a separate company basis), and the denominator of which is the sum of the amounts of the net BIE of each CFC group member with net BIE (computed on a separate company basis).

After applying the CFC group rules to determine each CFC group member's allocable share of the CFC group's applicable net BIE, each CFC group member that has BIE is required to perform a stand-alone section 163(j) calculation to determine whether any BIE is disallowed under the section 163(j) limitation.

3. Membership in a CFC Group

Under the 2018 Proposed Regulations, in general, a CFC group means two or more applicable CFCs if at least 80 percent of the value of the stock of each applicable CFC is owned, within the meaning of section 958(a), by a single U.S. shareholder or, in the aggregate, by related U.S. shareholders that own stock of each member in the same proportion. The 2018 Proposed Regulations also generally treat a controlled partnership (in general, a partnership in which CFC group members own, in the aggregate, at least 80 percent of the interests) as a CFC group member. For purposes of identifying a CFC group, members of a consolidated group are treated as a single person, as are individuals filing a joint return, and stock owned by certain passthrough entities is treated as owned proportionately by the owners or beneficiaries of the passthrough entity.

The 2018 Proposed Regulations exclude from the definition of a CFC group member an applicable CFC that has any income that is effectively connected with the conduct of a trade or business in the United States. In addition, if one or more CFC group members conduct a financial services business, those entities are treated as comprising a separate subgroup.

Under the 2018 Proposed Regulations, a CFC group election is made by applying the rules applicable to CFC groups for purposes of computing each CFC group member's deduction for BIE. Once made, the CFC group election is irrevocable.

4. Roll-Up of CFC Excess Taxable Income to Other CFC Group Members and U.S. Shareholders

Under the 2018 Proposed Regulations, if a CFC group election is in effect with respect to a CFC group, then an upper-tier CFC group member takes into account a proportionate share of any ''CFC excess taxable income'' of a lower-tier CFC group member in which it directly owns stock for purposes of computing the upper-tier member's ATI. The meaning of the term ''CFC excess taxable income'' is analogous to the meaning of the term ''excess taxable income'' in the context of a partnership and S corporation, and, in general, means the amount of a CFC group member's ATI in excess of the amount needed to prevent any BIE of the CFC group member from being disallowed under section 163(j).

Under the 2018 Proposed Regulations, a U.S. shareholder is not permitted to include in its ATI amounts included in gross income under section 951(a) (subpart F inclusions), section 951A(a) (GILTI inclusions), or section 78 (section 78 inclusions) that are properly allocable to a non-excepted trade or business (collectively, deemed income inclusions). However, the 2018 Proposed Regulations provide that a portion of CFC excess taxable income of the highest-tier applicable CFC is permitted to be used to increase the ATI of its U.S. shareholders. That portion is equal to the U.S. shareholder's interest in the highest-tier applicable CFC multiplied by its specified ETI ratio. The numerator of the specified ETI ratio is the sum of the U.S. shareholder's income inclusions under sections 951(a) and 951A(a) with respect to the specified highest-tier member and specified lower-tier members, and the denominator is the sum of the taxable income of the specified highest-tier member and specified lower-tier members.

B. Summary of Comments on Proposed § 1.163(j)–7 Contained in the 2018 Proposed Regulations

The Treasury Department and the IRS requested comments in the preamble to the 2018 Proposed Regulations regarding whether it would be appropriate to further modify the application of section 163(j) to applicable CFCs and whether there are particular circumstances in which it may be appropriate to exempt an applicable CFC from the application of section 163(j). Some commenters recommended that section 163(j) not apply to applicable CFCs. Those comments are addressed in part VIII of the Summary of Comments and Explanation of Revisions section in the Final Regulations.

A number of commenters broadly requested changes to the roll-up of CFC excess taxable income. Many of these commenters expressed concern about the administrability of rolling up CFC excess taxable income. Some commenters suggested that the CFC group election be available to a stand-alone applicable CFC in order to allow its CFC excess taxable income to be used to increase the ATI of a U.S. shareholder, or that an applicable CFC be permitted to use any CFC excess taxable income to increase the ATI of a shareholder without regard to whether it is a CFC group member. Furthermore, some commenters asserted that the nature of the roll-up compels multinationals to restructure their operations in order to move CFCs with relatively high amounts of ATI and low amounts of interest expense to the bottom of the ownership chain and CFCs with relatively low amounts of ATI and high amounts of interest expense to the top of the ownership chain, in order to maximize the benefits of the roll-up of CFC excess taxable income.

Some commenters asserted that because multinational organizations may own hundreds of CFCs, applying the section 163(j) limitation on a CFC-by-CFC basis, without regard to whether a CFC group election has been made under the 2018 Proposed Regulations, represents a significant administrative burden. Many comments suggested that CFC groups should be permitted to apply section 163(j) on a group basis, with a single group-level section 163(j) calculation similar to the rules applicable to a consolidated group. A few commenters suggested that this rule should be applied in addition to the roll-up of CFC excess taxable income, but most commenters recommended that the group rule be applied instead of the roll-up.

A number of commenters asserted that the requirements to be a member of a CFC group under the 2018 Proposed Regulations are overly restrictive. Some of these commenters recommended that the 80-percent ownership threshold be replaced with the ownership requirements of affiliated groups under section 1504(a), the rules of which are well-known and understood. Others recommended that the 80-percent ownership requirement be reduced to 50 percent, consistent with the standard for treatment of a foreign corporation as a CFC. Still others asserted that U.S. shareholders owning stock in applicable CFCs should not each be required to own the same proportion of stock in each applicable CFC in order for their ownership interests to count towards the 80-percent ownership requirement, or that the attribution rules of section 958(b), rather than section 958(a), should apply for purposes of determining whether the ownership requirements are met. Finally, some of these commenters requested that a CFC group election be permitted when one applicable CFC meets the ownership requirements for other applicable CFCs, even if no U.S. shareholder meets the ownership requirements for a highest-tier applicable CFC.

Some commenters requested the CFC financial services subgroups not be segregated from the CFC group and their BIE and BII be included in the general CFC group.

Some commenters requested that an applicable CFC with effectively connected income be permitted to be a member of a CFC group and that only its effectively connected income items should be excluded. Alternatively, commenters requested a de minimis rule that would permit an applicable CFC to be a member of a CFC group if the applicable CFC's effectively connected income is below a certain threshold of total income, such as 10 percent.

Some commenters requested that the CFC group election be revocable. The commenters proposed either making the CFC group election an annual election or providing that the election applies for a certain period, for example, three or five years, before it can be revoked.

Finally, commenters requested a safe harbor or exclusion providing that if a CFC group would not be limited under section 163(j) either because the CFC group has no net BIE or because its BIE does not exceed 30 percent of the CFC group's ATI, a U.S. shareholder would not have to apply section 163(j) for the applicable CFC or be subject to applicable CFC section 163(j) reporting requirements.

C. Proposed § 1.163(j)–7

1. Overview

As noted in the preamble to the Final Regulations, the Treasury Department and the IRS have determined, based on a plain reading of section 163(j) and § 1.952–2, that section 163(j) applies to foreign corporations where relevant under current law and has applied to such corporations since the effective date of the new provision.[1] Congress

[1] Section 1.952–2(b) generally provides that the taxable income for a foreign corporation is determined by treating the foreign corporation as a

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expressly provided that section 163(j) should not apply to certain small businesses or to certain excepted trades or businesses. Nothing in the Code or legislative history indicates that Congress intended to except other persons with trades or businesses, as defined in section 163(j)(7), from the application of section 163(j). Accordingly, the Treasury Department and the IRS have determined that, consistent with a plain reading of section 163(j) and § 1.952–2, it is appropriate for section 163(j) to apply to applicable CFCs and other foreign corporations whose taxable income is relevant for Federal tax purposes (other than by reason of having ECI or income described in section 881 (FDAP)) (relevant foreign corporations).[2] In the case of CFCs with ECI, see proposed § 1.163(j)–8. For further discussion of the Treasury Department and the IRS's determination that there is not a statutory basis for exempting applicable CFCs from the application of section 163(j), see part VIII of the Summary of Comments and Explanation of Revisions section of the Final Regulations.

A number of comments were received asserting that there are other mechanisms that eliminate the policy need for section 163(j) to apply to limit leverage in CFCs. For example, some commenters have cited tax rules in foreign jurisdictions limiting interest deductions, including thin capitalization rules (or similar rules intended to implement the Organisation for Economic Co-operation and Development (OECD) recommendations under Action 4 of the Base Erosion and Profits Shifting Project). The Treasury Department and the IRS disagree with these assertions. The Treasury Department and the IRS note that these rules are not universally applied in other jurisdictions, that many jurisdictions do not have any meaningful interest expense limitation rules, and that some jurisdictions have no interest expense limitation rules of any kind.

Even if some CFCs owned by a U.S. shareholder are in foreign jurisdictions with meaningful thin capitalization rules, in the absence of section 163(j), it would still be possible to use leverage to reduce or eliminate a U.S. shareholder's global intangible low-taxed income (GILTI) under section 951A for these CFCs. This is because for purposes of computing a U.S. shareholder's GILTI under section 951A, tested income of CFCs may be offset by tested losses of CFCs owned by the U.S. shareholder. See section 951A(c). The ability to deduct interest without limitation under section 163(j) would result in tested losses in CFCs with significant leverage. Because of this aggregation, one overleveraged CFC in a single jurisdiction that does not have rules limiting interest expense can, without the application of section 163(j), reduce or eliminate tested income from all CFCs owned by a U.S. shareholder regardless of jurisdiction.

Other comments suggested that, to the extent that debt of a CFC is held by a related party, transfer pricing principles would discipline the amount of interest expense. Comments also note that to the extent that debt of a CFC is held by a third party, market forces would discipline the leverage present in the CFC. While both of these concepts may discipline the amount of leverage present in a CFC, they would also discipline the amount of leverage in any entity. If Congress believed that market forces and transfer pricing principles were sufficient disciplines to prevent overleverage, section 163(j) would not have been amended as part of TCJA to clearly apply to interest expense paid or accrued to both third parties and related parties. In addition, if transfer pricing were sufficient to police interest expense in the related party context, old section 163(j) (as enacted in 1989 and subsequently revised prior to TCJA) would not have been necessary.

However, the Treasury Department and the IRS also have determined that it is appropriate, while still carrying out the provisions of the statute and the policies of section 163(j), to reduce the administrative and compliance burdens of applying section 163(j) to applicable CFCs. Accordingly, Proposed § 1.163(j)–7 allows for an election to be made to apply section 163(j) on a group basis with respect to applicable CFCs that are ''specified group members'' of a ''specified group.'' If the election is made, the specified group members are referred to as ''CFC group members'' and all of the CFC group members collectively are referred to as a ''CFC group.'' The rules for determining a specified group and specified group members are discussed in part V.C.3. of this Explanation of Provisions section. The rules and procedures for treating specified group members as CFC group members and for determining a CFC group are discussed in part V.C.4. of this Explanation of Provisions section.

In addition, Proposed § 1.163(j)–7 provides a safe harbor election that exempts certain applicable CFCs from application of section 163(j). The safe-harbor election is available for stand-alone applicable CFCs (which is an applicable CFC that is not a specified group member of a specified group) and CFC group members. The election is not available for an applicable CFC that is a specified group member but not a CFC group member because a CFC group election is not in effect. See part V.C.7. of this Explanation of Provisions section.

Proposed § 1.163(j)–7 also provides an anti-abuse rule that increases ATI in certain circumstances.

Finally, Proposed § 1.163(j)–7 allows a U.S. shareholder of a stand-alone applicable CFC or a CFC group member of a CFC group to include a portion of its deemed income inclusions attributable to the applicable CFC in the U.S. shareholder's ATI. This rule does not apply with respect to an applicable CFC that is a specified group member but not a CFC group member because a CFC group election is not in effect. See part V.C.9. of this Explanation of Provisions section.

The Treasury Department and the IRS anticipate that, in many instances, Proposed § 1.163(j)–7 will significantly reduce the administrative and compliance burdens of applying section 163(j) to applicable CFCs relative to the 2018 Proposed Regulations.

Unlike Proposed § 1.163(j)–8, which provides rules for allocating disallowed BIE to ECI and non-ECI, Proposed § 1.163(j)–7 does not allocate disallowed BIE among classes of income. The Treasury Department and the IRS request comments on appropriate methods of allocating disallowed BIE among classes of income, such as subpart F income, as defined in section 952, and tested income, as defined in section 951A(c)(2)(A) and § 1.951A–2(b)(1), as well as comments on whether and the extent to which rules implementing such methods may be necessary.

In addition, the Treasury Department and the IRS request comments on appropriate methods of allocating disallowed BIE for other purposes, including between items described in § 1.163(j)–1(b)(22)(i) and other items described in § 1.163(j)–1(b)(22) (defining interest), as well as comments on whether and the extent to which rules implementing such methods may be necessary.

The Treasury Department and the IRS do not anticipate that section 163(j) will affect the tax liability of a passive foreign investment company, within the

domestic corporation but with certain enumerated exceptions. Section 1.952–2(c) provides for a number of exceptions, but none of the exceptions affects the application of section 163(j).

[2] For purposes of Proposed § 1.163(j)–7, the term effectively connected income (or ECI) means income or gain that is ECI, as defined in § 1.884–1(d)(1)(iii), and deduction or loss that is allocable to, ECI, as defined in § 1.884–1(d)(1)(iii).

meaning of section 1297(a) (PFIC), or its shareholders, solely because the PFIC is a relevant foreign corporation. See § 1.163(j)–4(c)(1) (providing that section 163(j) does not affect earnings and profits). The Treasury Department and the IRS request comments on whether any additional guidance is needed to reduce the compliance burden of section 163(j) on PFICs and their shareholders.

2. Application of Section 163(j) to CFC Group Members

a. Single Section 163(j) Limitation for a CFC Group

Proposed § 1.163(j)–7(c) provides rules for applying section 163(j) to CFC group members of a CFC group. Under the Proposed Regulations, a single section 163(j) limitation is computed for a CFC group. See proposed § 1.163(j)–7(c)(2). For this purpose, the current-year BIE, disallowed BIE carryforwards, BII, floor plan financing interest expense, and ATI of a CFC group are equal to the sums of the current-year amounts of such items for each CFC group member for its specified taxable year with respect to the specified period. (The terms ''specified taxable year'' and ''specified period'' are discussed in part V.C.3. of this Explanation of Provisions section.) A CFC group member's current-year BIE, BII, floor plan financing interest expense, and ATI for a specified taxable year are generally determined on a separate-company basis before being included in the CFC group calculation.

b. Allocation of CFC Group's Section 163(j) Limitation to Business Interest Expense of CFC Group Members

The extent to which a CFC group's section 163(j) limitation is allocated to a particular CFC group member's current-year BIE and disallowed BIE carryforwards is determined using the rules that apply to consolidated groups under § 1.163(j)–5(a)(2) and (b)(3)(ii) (consolidated BIE rules), subject to certain modifications. See proposed § 1.163(j)–7(c)(3)(i). Because many CFC groups will be owned by consolidated groups, many taxpayers will be familiar with the consolidated BIE rules.

If the sum of the CFC group's current-year BIE and disallowed BIE carryforwards exceeds the CFC group's section 163(j) limitation, then current-year BIE is deducted first. If the CFC group's current-year BIE exceeds the CFC group's section 163(j) limitation, then each CFC group member deducts the amount of its current-year BIE not in excess of the sum of its BII and floor plan financing interest expense, if any. Then, if the CFC group has any section 163(j) limitation remaining for the current year, each applicable CFC with remaining current-year BIE deducts a pro rata portion thereof.

If the CFC group's section 163(j) limitation exceeds its current-year BIE, then CFC group members may deduct all of their current-year BIE and may deduct disallowed BIE carryforwards not in excess of the CFC group's remaining section 163(j) limitation. The disallowed BIE carryforwards are deducted in the order of the taxable years in which they arose, beginning with the earliest taxable year, and disallowed BIE carryforwards that arose in the same taxable year are deducted on a pro rata basis. This taxable year ordering rule is consistent with the consolidated BIE rules. However, Proposed § 1.163(j)–7 provides special rules for disallowed BIE carryforwards when CFC group members have different taxable years, or a CFC group member has multiple taxable years with respect to the specified period of the CFC group. Unlike members of a consolidated group, not all CFC group members will have the same taxable years, and not all CFC group members will have the same taxable year as the parent of the CFC group. As discussed in part V.C.3 of this Explanation of Provisions section, a CFC group member is included in a CFC group for its entire taxable year that ends with or within a specified period.[3]

c. Limitation on Pre-Group Disallowed Business Interest Expense Carryforwards

The disallowed BIE carryforwards of a CFC group member when it joins a CFC group (pre-group disallowed BIE carryforwards) are subject to the same CFC group section 163(j) limitation and are deducted pro rata with other CFC group disallowed BIE carryforwards. However, pre-group disallowed BIE carryforwards are subject to additional limitations, similar to the limitations on deducting the disallowed BIE carryforwards of a consolidated group arising in a SRLY, as defined in § 1.1502–1(f), or treated as arising in a SRLY under the principles of § 1.1502–21(c) and (g). The policy of the limitation imposed on pre-group BIE carryforwards is analogous to the policy of the SRLY limitation for consolidated groups.

The rules and principles of § 1.163(j)–5(d)(1)(B), which applies SRLY subgroup principles to disallowed BIE carryforwards of a consolidated group, apply to pre-group subgroups. If a CFC group member with pre-group disallowed BIE carryforwards (loss member) leaves one CFC group (former group) and joins another CFC group (current group), the loss member and each other CFC group member that left the former group and joined the current group for a specified taxable year with respect to the same specified period consists of a ''pre-group subgroup.'' Unlike SRLY subgroups, it is not required that all members of a pre-group subgroup join the CFC group at the same time, since each applicable CFC that joins a CFC group is treated as joining on the first day of its taxable year. As a result, even if multiple applicable CFCs are acquired on the same day in a single transaction, they would join the CFC group on different days if they have different taxable years.

d. Special Rules for Specified Periods Beginning in 2019 or 2020

Proposed § 1.163(j)–7(c)(5) provides special rules for applying section 163(j)(10) to CFC groups. The proposed regulations provide that elections under section 163(j)(10) are made for a CFC group (rather than for each CFC group member). For a specified period of a CFC group beginning in 2019 or 2020, unless the election described in § 1.163(j)–2(b)(2)(ii)(A) is made, the CFC group section 163(j) limitation is determined by using 50 percent (rather than 30 percent) of the CFC group's ATI for the specified period, without regard to whether the taxable years of CFC group members begin in 2019 or 2020. If the election described in § 1.163(j)–2(b)(2)(ii)(A) is made for a specified period of a CFC group, the CFC group section 163(j) limitation is determined by using 30 percent (rather than 50 percent) of the CFC group's ATI for the specified period, without regard to whether the taxable years of CFC group members begin in 2019 or 2020. The election is made for the CFC group by each designated U.S. person.

[3] For example, assume a U.S. multinational group parented by a consolidated group with a taxable year that is the calendar year includes applicable CFCs with November 30 taxable years and other applicable CFCs with calendar year taxable years. In this case, as discussed in more detail in part V.C.3.b. of the Explanation of Provisions section, the specified period of the CFC group for 2020 would begin on January 1, 2020, and end on December 31, 2020. Furthermore, the specified taxable year of a CFC group member with a taxable year that is the calendar year is its taxable year ending December 31, 2020, and the specified taxable year of a CFC group member with a November 30 taxable year is its taxable year ending November 30, 2020 (the taxable years that end with or within the specified period). A CFC group member can also have multiple taxable years with respect to a specified period. For example, a CFC group member may have a short taxable year due to an election under § 1.245A–5T(e)(3)(i) (elective exception to close a CFC's taxable year in the case of an extraordinary reduction).

The election under § 1.163(j)–2(b)(3)(i) to use 2019 ATI (that is, ATI for the last taxable year beginning in 2019) rather than 2020 ATI (that is, ATI for a taxable year beginning in 2020) is made for a specified period of a CFC group beginning in 2020 (2020 specified period) and applies to the specified taxable years of CFC group members with respect to the 2020 specified period. Accordingly, if a specified taxable year of a CFC group member with respect to a CFC group's 2020 specified period begins in 2020, then the election is applied to such taxable year using the CFC group member's ATI for its last taxable year beginning in 2019. In some cases, the specified taxable year of a CFC group member with respect to a CFC group's 2020 specified period will begin in 2019 or 2021. If the specified taxable year of the CFC group member begins in 2019, then the election is applied to such taxable year using the CFC group member's ATI for its last taxable year beginning in 2018; if the specified taxable year of the CFC group member begins in 2021, then the election is applied to such taxable year using the CFC group member's ATI for its last taxable year beginning in 2020.

For example, assume a CFC group has two CFC group members, CFC1 and CFC2, and has a specified period that is the calendar year. CFC1 has a taxable year that is the calendar year, and CFC2 has a taxable year that ends November 30. The election under § 1.163(j)–2(b)(3)(i) is in effect for the specified period beginning January 1, 2020, and ending December 31, 2020 (which is the 2020 specified period). As a result, the ATI of the CFC group for the 2020 specified period is determined by reference to the specified taxable year of CFC1 beginning January 1, 2019, and ending December 31, 2019 (the last taxable year beginning in 2019), and the specified taxable year of CFC2 beginning December 1, 2018, and ending November 30, 2019 (the last taxable year beginning in 2018).

Alternatively, assume (i) the same CFC group instead has a 2020 specified period that begins on December 1, 2020, and ends on November 30, 2021; (ii) in 2019 and 2020, CFC1 has a taxable year that is the calendar year, but in 2021, CFC1 has a short taxable year that begins on January 1, 2021, and ends on June 30, 2021; and (iii) CFC2 has a taxable year ending November 30 (for all years). Further assume that the election under § 1.163(j)–2(b)(3)(i) is in effect for the 2020 specified period. In this case, the election applies to the specified taxable year of CFC1 that begins on January 1, 2020, and ends on December 31, 2020; the specified taxable year of CFC1 that begins on January 1, 2021, and ends on June 30, 2021; and the specified taxable year of CFC2 that begins on December 1, 2020, and ends on November 30, 2021. As a result of the election, the ATI of the CFC group for the 2020 specified period is determined by reference to the specified taxable year of CFC1 beginning January 1, 2019, and ending December 31, 2019, the specified taxable year of CFC1 beginning January 1, 2020, and ending December 31, 2020, and the specified taxable year of CFC2 beginning December 1, 2019, and ending November 30, 2020.

If the election under § 1.163(j)–2(b)(3)(i) to use 2019 ATI rather than 2020 ATI is made for a CFC group, the CFC group's ATI for the 2020 specified period is determined by reference to the 2019 ATI of all CFC group members (except to the extent that 2018 or 2020 ATI is used, as described earlier), including any CFC group member that joins the CFC group during the 2020 specified period. Therefore, a CFC group's ATI for the 2020 specified period may be determined by reference to a prior taxable year of a new CFC group member even though the CFC group member was not a CFC group member in the prior taxable year. If a CFC group member leaves the CFC group during the 2020 specified period, the ATI of the CFC group for the 2020 specified period is determined without regard to the ATI of the departing CFC group member.

As stated in the Background section of this preamble, Revenue Procedure 2020–22 generally provides the time and manner of making or revoking elections under section 163(j)(10), including elections with respect to applicable CFCs. References in Revenue Procedure 2020–22 to CFC groups and CFC group members are to CFC groups and applicable CFCs for which a CFC group election is made under the 2018 Proposed Regulations. The rules described in this part V.C.2.d of this Explanation of Provisions section and proposed § 1.163(j)–7(c)(5) modify the application of Revenue Procedure 2020–22 and the elections under section 163(j)(10) for CFC groups and applicable CFCs for which a CFC group election is made under Proposed § 1.163(j)–7.

Thus, for example, if a CFC group has two designated U.S. persons that are U.S. corporations, pursuant to proposed § 1.163(j)–7(c)(5), the election to not apply the 50 percent ATI limitation to the CFC group for a specified period beginning in 2020 is made for the specified period of the CFC group by each designated U.S. person, and pursuant to Revenue Procedure 2020–22, section 6.01(2), the election to not apply the 50 percent ATI limitation is made by the each designated U.S. person timely filing a Federal income tax return, including extensions, using the 30 percent ATI limitation for purposes of determining the taxable income of the CFC group.

For purposes of applying § 1.964–1(c), the elections described in proposed § 1.163(j)–7(c)(5) are treated as if made for each CFC group member. Thus, the requirements to provide a statement and written notice as provided under § 1.964–1(c)(3)(i)(B) and (C) apply.

3. Specified Groups and Specified Group Members

a. In General

Proposed § 1.163(j)–7(d) provides rules for determining a specified group and specified group members. The determination of a specified group and specified group members is the basis for determining a CFC group and CFC group members. This is because a CFC group member is a specified group member of a specified group for which a CFC group election is in effect, and a CFC group consists of all the CFC group members. See proposed § 1.163(j)–7(e)(2).

b. Specified Group

Under proposed § 1.163(j)–7(d)(2), a specified group includes one or more chains of applicable CFCs connected through stock ownership with a specified group parent, but only if the specified group parent owns stock meeting the requirements of section 1504(a)(2)(B) (pertaining to value) in at least one applicable CFC, and stock meeting the requirements of section 1504(a)(2)(B) in each of the applicable CFCs (except the specified group parent) is owned by one or more of the other applicable CFCs or the specified group parent.

Unlike the general rules in section 1504, in order to avoid breaking affiliation with a partnership or foreign trust or foreign estate, for purposes of determining whether stock in an applicable CFC meeting the requirements of section 1504(a)(2)(B) is owned by the specified group parent or other applicable CFCs, proposed § 1.163(j)–7(d)(2) takes into account both stock owned directly and stock owned indirectly under section 318(a)(2)(A) through a domestic or foreign partnership or under section 318(a)(2)(A) or (a)(2)(B) through a foreign estate or trust (the look-through rule). For example, assume CFC1 and CFC2 is each an applicable CFC and a specified group member of a specified group. If CFC1 and CFC2 each own 50 percent of the capital and profits interests in a partnership, and the partnership wholly owns CFC3, an applicable CFC, then, by reason of the look-through rule, CFC3 is also included in the specified group, although the partnership is not.

The specified group rules also differ from the affiliated group rules in section 1504 in that they require only that 80 percent of the total value (pursuant to section 1504(a)(2)(B)), not 80 percent of both vote and value (pursuant to section 1504(a)(2)(A) and (a)(2)(B)), of an applicable CFC be owned by the specified group parent or other applicable CFCs in the specified group in order for the applicable CFC to be included in the specified group. The Treasury Department and the IRS determined that limiting the 80-percent threshold to value is appropriate to prevent taxpayers from breaking affiliation by diluting voting power below 80 percent.

The specified group has a single specified group parent, which may be either a qualified U.S. person or an applicable CFC. However, the specified group parent is included in the specified group only if it is an applicable CFC. For this purpose, a *qualified U.S. person* means a U.S. person that is a citizen or resident of the United States or a domestic corporation. For purposes of determining the specified group parent, members of a consolidated group are treated as a single corporation and individuals whose filing status is ''married filing jointly'' are treated as a single individual (aggregation rule). The Treasury Department and the IRS have determined that the aggregation rule is appropriate because all deemed inclusions with respect to applicable CFCs included in gross income of members of a consolidated group or of individuals filing a joint return, as applicable, are reported on a single U.S. tax return. The Treasury Department and the IRS determined that it is appropriate for an S corporation to be a qualified U.S. person because an S corporation can have only a single class of stock and therefore the economic rights of its shareholders in all applicable CFCs owned by the S corporation are proportionate to share ownership. On the other hand, the Treasury Department and the IRS have determined that it is not appropriate for a domestic partnership to be a qualified U.S. person because of the ability of partnerships to make disproportionate or special allocations and therefore the economic rights of partners in the partnership with respect to all applicable CFCs owned by a partnership will not necessarily be proportionate to ownership. However, if, for example, a domestic partnership wholly owns an applicable CFC, which wholly owns multiple other applicable CFCs, and no qualified U.S. person owns stock in the top-tier CFC meeting the requirements of section 1504(a)(2)(B), taking into account the look-through rule, then the applicable CFCs are included in a specified group of which the top-tier CFC is the specified group parent.

The Treasury Department and the IRS request comments regarding whether, and to what extent, the definition of a ''qualified U.S. person'' should be expanded to include domestic estates and trusts or whether and to what extent the look-through rule should apply if stock of applicable CFCs is owned by domestic estates and trusts.

Each specified group has a specified period. A specified period is similar to a taxable year but determined with respect to a specified group. A specified group does not have a taxable year because the specified group members may not have the same taxable year. If the specified group parent is a qualified U.S. person, the specified period generally ends on the last day of the taxable year of the specified group parent and begins on the first day after the last day of the prior specified period. Thus, for example, if the specified group parent is a domestic corporation with a calendar year taxable year, the specified period generally begins on January 1 and ends on December 31. If the specified group parent is an applicable CFC, the specified period generally ends on the last day of the required year of the specified group parent, determined under section 898(c)(1), without regard to section 898(c)(2), and begins on the first day after the last day of the prior specified period. However, a specified period never begins before the first day on which the specified group exists or ends after the last day on which the specified group exists. Like a taxable year, a specified period can never be longer than 12 months.

The principles of § 1.1502–75(d)(1), (d)(2)(i) through (d)(2)(ii), and (d)(3)(i) through (d)(3)(iv) (regarding when a consolidated group remains in existence) (§ 1.1502–75(d) principles) apply for purposes of determining when a specified group ceases to exist. Solely for purposes of applying the § 1.1502–75(d) principles, each applicable CFC that is treated as a specified group member for a taxable year of the applicable CFC with respect to a specified period is treated as affiliated with the specified group parent from the beginning to the end of the specified period, without regard to the beginning or end of its taxable year. This rule does not affect the general rule that, for purposes other than § 1.1502–75(d) (such as the application of section 163(j) to a CFC group), an applicable CFC is a specified group member with respect to a specified period for its taxable year ending with or within the specified period.[4]

The Treasury Department and the IRS request comments as to whether any modifications to the § 1.1502–75(d) principles should be made for specified groups.

c. Specified Group Members

Proposed § 1.163(j)–7(d)(3) provides rules for determining specified group members with respect to a specified group. The determination as to whether an applicable CFC is a specified group member is made with respect to a taxable year of the applicable CFC and specified period of a specified group. Specifically, if the applicable CFC is included in a specified group on the last day of its taxable year that ends with or within the specified period, the applicable CFC is a specified group member with respect to the specified period for the entire taxable year.[5]

[4] For example, assume a specified group parent with a specified period that is the calendar year acquires all of the stock of CFC1, an applicable CFC, on June 30, Year 1, and sells all of the stock of CFC1 on June 30, Year 3. CFC1 has a November 30 taxable year, and the specified period is the calendar year. CFC1 is included in the specified group on November 30, Year 1, and November 30, Year 2 (but not November 30, Year 3). As a result, CFC1 is a specified group member for its taxable year ending November 30, Year 1, with respect to the specified period ending December 31, Year 1, and for its taxable year ending November 30, Year 2, with respect to the specified period ending December 31, Year 2. Solely for purposes of applying the § 1.1502–75(d) principles, CFC1 is treated as affiliated with the specified group parent from the beginning to the end of the specified period ending December 31, Year 1, and from the beginning to the end of the specified period ending December 31, Year 2. In other words, CFC1 is treated as affiliated with the specified group parent from January 1, Year 1, to December 31, Year 2.

[5] For example, assume CFC1, an applicable CFC, has a taxable year beginning December 1, Year 1, and ending November 30, Year 2, and a specified group has a specified period beginning January 1, Year 2, and ending December 31, Year 2. If CFC1 is included in the specified group on November 30, Year 2, then CFC1 is a specified group member with respect to the specified period for its entire taxable year ending November 30, Year 2. This is the case even if CFC1 is not included in the specified group during part of its taxable year ending November 30, Year 2 (for example, because all of the stock of CFC2 is purchased by the specified group on June 1, Year 2, and its taxable year does not close as a result of joining the specified group), or if CFC1 ceases to be included in the specified group after November 30, Year 2, but before December 31, Year 2 (for example, because all of the stock of CFC1 is

Continued

The Treasury Department and the IRS are concerned about the potential for abuse that may arise if taxpayers cause an applicable CFC that otherwise would be treated as a specified group member and a CFC group member to avoid being treated as a CFC group member. For example, the Treasury Department and the IRS have determined that it is not appropriate for taxpayers to prevent an applicable CFC with high ATI and low BIE from being part of a CFC group with a goal of increasing its CFC excess taxable income and its U.S. shareholders' ATI inclusions, rather than allowing the applicable CFC's ATI to be used by the CFC group. The Treasury Department and the IRS request comments on appropriate methods of preventing an applicable CFC from avoiding being a CFC group member for purposes of increasing the ATI of its U.S. shareholders. The Treasury Department and the IRS also request comments on whether a rule similar to the rule in section 1504(a)(3), which prevents domestic corporations from rejoining a consolidated group for 60 months, should apply to prevent applicable CFCs from rejoining a CFC group.

4. CFC Groups and CFC Group Members

a. In General

Proposed § 1.163(j)–7(e) provides rules and procedures for treating specified group members as CFC group members and for determining a CFC group. A CFC group member means a specified group member of a specified group for which a CFC group election is in effect. The specified group member is a CFC group member for a specified taxable year with respect to a specified period. A CFC group means all CFC group members for their specified taxable years with respect to a specified period. See proposed § 1.163(j)–7(e)(2) (defining CFC group and CFC group member). Thus, if a CFC group election is in place, the terms ''specified group members,'' ''CFC group members,'' and a ''CFC group'' refer to the same applicable CFCs. The term ''specified group,'' which is determined at any moment in time, may not necessarily refer to the exact same applicable CFCs.

Once a CFC group election is made, the CFC group continues until the CFC group election is revoked or until the end of the last specified period with respect to the specified group. See proposed § 1.163(j)–7(e)(3). When a CFC group election is in effect, if an applicable CFC becomes a specified group member with respect to a specified period of the specified group, the CFC group election applies to the applicable CFC and it becomes a CFC group member. When an applicable CFC ceases to be a specified group member with respect to a specified period of a specified group, the CFC group election terminates solely with respect to the applicable CFC. See proposed § 1.163(j)–7(e)(4) (joining or leaving a CFC group).

b. Making or Revoking a CFC Group Election

Proposed § 1.163(j)–7(e)(5) provides rules for making and revoking a CFC group election. Proposed § 1.163(j)–7(e)(5)(i) provides that a CFC group election applies with respect to a specified period of a specified group. Accordingly, the CFC group election applies to each specified group member for its entire specified taxable year that ends with or within the specified period. In response to comments to the 2018 Proposed Regulations, the CFC group election is not irrevocable. Instead, once made, a CFC group election cannot be revoked with respect to any specified period of the specified group that begins during the 60-month period following the last day of the first specified period for which the election was made. Similarly, once revoked, a CFC group election cannot be made again with respect to any specified period of the specified group that begins during the 60-month period following the last day of the first specified period for which the election was revoked.

The Treasury Department and the IRS request comments regarding whether a specified group that does not make a CFC group election when it first comes into existence (or for the first specified period following 60 days after the date of publication of the Treasury decision adopting these regulations as final in the **Federal Register**) should be prohibited from making the CFC group election for any specified period beginning during the 60-month period following that specified period.

Thus, under the Proposed Regulations, in the case of a specified group, taxpayers choose to apply section 163(j) to specified group members on a CFC group basis or on a stand-alone basis for no less than a 60-month period. The Treasury Department and the IRS have determined that a 60-month period is an appropriate balance between making the choice irrevocable and providing an annual election, the latter of which may facilitate inappropriate tax planning (in this regard, see, for example, the discussion in part C.7 of this part V of the Explanation of Provisions section).

c. Specified Financial Services Subgroup Rules

In response to comments, Proposed § 1.163(j)–7 does not provide for CFC financial services subgroups. Instead, applicable CFCs that otherwise qualify as CFC group members are treated as part of the same CFC group.

d. Interaction of the CFC Group Election in Proposed § 1.163(j)–7 With the CFC Group Election in the 2018 Proposed Regulations

The CFC group election can be made only in accordance with the method prescribed in proposed § 1.163(j)–7(e)(5). The 2018 Proposed Regulations also contained an election called a ''CFC group election'' (old CFC group election). The old CFC group election is a different election than the CFC group election contained in Proposed § 1.163(j)–7. Accordingly, the old CFC group election may be relied on only for taxable years in which the taxpayer relies on the 2018 Proposed Regulations. Whether an old CFC group election was made under the 2018 Proposed Regulations has no effect on whether a CFC group election under proposed § 1.163(j)–7(e)(5) is in effect for any taxable year in which the taxpayer relies on Proposed § 1.163(j)–7.

5. Exclusion of ECI From Application of Section 163(j) to a CFC Group

In response to comments, proposed § 1.163(j)–7 provides that an applicable CFC with ECI is not precluded from being a CFC group member. However, under proposed § 1.163(j)–7(f), only the ATI, BII, BIE, and floor plan financing of the applicable CFC that are not attributable to ECI are included in the CFC group's section 163(j) calculations. The ECI items of the applicable CFC are not included in the CFC group calculations. Instead, the ECI of the applicable CFC is treated as income of a separate CFC, an ''ECI deemed corporation,'' that has the same taxable year and shareholders as the applicable CFC, but that is not a CFC group member. The ECI deemed corporation must do a separate section 163(j) calculation for its ECI in accordance with Proposed § 1.163(j)–8. See Proposed § 1.163(j)–8 and part VI of this Explanation of Provisions section for rules applicable to foreign corporations with ECI.

6. Treatment of Foreign Taxes for Purposes of Computing ATI

Proposed § 1.163(j)–7(g)(3) provides that, for purposes of computing its ATI, tentative taxable income of a relevant foreign corporation is determined by taking into account a deduction for

sold by the specified group on December 15, Year 2).

foreign taxes. This rule is consistent with § 1.952–2, which provides that the taxable income of a foreign corporation for any taxable year is determined by treating the foreign corporation as a domestic corporation, and section 164(a), which allows a deduction for foreign taxes. The Treasury Department and the IRS request comments regarding whether, and the extent to which, the ATI of a relevant foreign corporation should be determined by adding to tentative taxable income any deductions for foreign income taxes.

7. Anti-Abuse Rule

The Treasury Department and the IRS are concerned that, in certain situations, U.S. shareholders may inappropriately affirmatively plan to limit BIE deductions as part of a tax-planning transaction, including by not making a CFC group election for purposes of increasing the disallowed BIE of a specified group member or of a partnership substantially owned by specified group members of the same specified group. For example, in a taxable year in which a U.S. shareholder would otherwise have foreign tax credits in the section 951A category in excess of the section 904 limitation, a U.S. shareholder might inappropriately cause one specified group member to pay interest to another specified group member in an amount in excess of the borrowing specified group member's section 163(j) limitation. As a result, the U.S. shareholder's pro rata share of tested income of the borrowing specified group member for the taxable year would be increased without increasing the U.S. shareholder's Federal income tax because excess foreign tax credits in the section 951A category in the taxable year that cannot be carried forward to a future taxable year would offset the Federal income tax on the incremental increase in the U.S. shareholder's pro rata share of tested income, while also enabling the borrowing specified group member to generate a disallowed BIE carryforward that may be used in a subsequent taxable year.

Accordingly, under proposed § 1.163(j)–7(g)(4), if certain conditions are met, when one specified group member or applicable partnership (specified borrower) pays interest to another specified group member or applicable partnership (specified lender), and the payment is BIE to the specified borrower and income to the specified lender, then the ATI of the specified borrower is increased by the amount necessary such that the BIE of the specified borrower is not limited under section 163(j). This amount is determined by multiplying the lesser of the payment amount or the disallowed BIE (computed without regard to this ATI adjustment) by 3⅓ (or by 2, in the case of taxable years or specified taxable years with respect to a specified period for which the section 163(j) limitation is determined by reference to 50 percent of ATI). A partnership is an applicable partnership if at least 80 percent of the capital or profits interests is owned, in aggregate, by direct or direct partners that are specified group members of the same specified group. The conditions for this rule to apply are as follows: (i) The BIE is incurred with a principal purpose of reducing the Federal income tax liability of a U.S. shareholder (including over multiple taxable years); (ii) the effect of the specified borrower treating the payment amount as disallowed BIE would be to reduce the Federal income tax of a U.S. shareholder; and (iii) either no CFC group election is in effect or the specified borrower is an applicable partnership.

8. The Safe-Harbor Election

Proposed § 1.163(j)–7(h) provides a safe-harbor election for stand-alone applicable CFCs and CFC groups. If the safe-harbor election is in effect for a taxable year, no portion of the BIE of the stand-alone applicable CFC or of each CFC group member, as applicable, is disallowed under the section 163(j) limitation. The safe-harbor election is an annual election. If the election is made, then no portion of any CFC excess taxable income is included in a U.S. shareholder's ATI. See proposed § 1.163(j)–7(j)(2)(iv).

The safe-harbor election cannot be made with respect to any foreign corporation that is not a stand-alone applicable CFC or a CFC group member. As a result, if a CFC group election is not in effect for a specified period, a specified group member of the specified group is not eligible for the safe-harbor election.

In the case of a stand-alone applicable CFC, the safe-harbor election may be made for a taxable year of the stand-alone applicable CFC if its BIE does not exceed 30 percent of the lesser of (i) its tentative taxable income attributable to non-excepted trades or businesses (referred to as ''qualified tentative taxable income''), and (ii) its ''eligible amount'' for the taxable year. In the case of a CFC group, the safe-harbor election may be made for the specified taxable years of each CFC group member with respect to a specified period if the CFC group's BIE does not exceed 30 percent of the lesser of (i) the sum of the qualified tentative taxable income of each CFC group member, and (ii) the sum of the eligible amounts of each CFC group member. For taxable years of a stand-alone applicable CFC or specified periods of a CFC group beginning in 2019 or 2020, the 30 percent limitation is replaced with a 50 percent limitation, consistent with the change in the section 163(j) limitation to take into account 50 percent, rather than 30 percent, of ATI for such taxable years or specified periods.

The ''eligible amount'' is a CFC-level determination. In general, the eligible amount is the sum of the applicable CFC's subpart F income plus the approximate amount of GILTI inclusions its U.S. shareholders would have were the applicable CFC wholly owned by domestic corporations that had no tested losses and that were not subject to the section 250(a)(2) limitation on the section 250(a)(1) deduction. Amounts used in the determination of the eligible amount are computed without regard to the application of section 163(j) and the section 163(j) regulations. While the eligible amount of an applicable CFC cannot be negative, qualified tentative taxable income can be negative. Thus, limiting the safe-harbor to 30 percent of qualified tentative taxable income ensures that losses of a stand-alone applicable CFC or a CFC group are taken into account in determining whether the stand-alone applicable CFC or the CFC group qualifies for the safe-harbor.[6]

The safe-harbor election does not apply to EBIE, as described in § 1.163(j)–6(f)(2), and EBIE is not taken into account for purposes of determining whether the safe-harbor election is available for a stand-alone applicable CFC or a CFC group, until such business interest expense is treated as paid or accrued by an applicable CFC in a succeeding year (that is, until the applicable CFC is allocated excess taxable income or excess business interest income from such partnership in accordance with § 1.163(j)–6(g)(2)(i)).

The safe-harbor election is intended to reduce the compliance burden on applicable CFCs that would not have disallowed BIE if they applied the

[6] For example, assume that, before taking into account BIE, a stand-alone applicable CFC has net income of $0x, consisting of $100x of subpart F income, a $100x loss attributable to foreign oil and gas extraction income, as defined in section 907(c)(1). It also has $20x of BIE, no BII, and no floor plan financing interest expense. The ATI of the CFC is zero and the section 163(j) limitation would be zero. However, the eligible amount of the CFC is $100x. Thus, absent a rule limiting the safe harbor to 30 percent of qualified tentative taxable income, the CFC would be permitted to deduct its $20x of business interest expense under the safe harbor, even though none of the BIE would be deductible under the section 163(j) limitation.

section 163(j) calculation. However, the Treasury Department and the IRS are concerned that the safe-harbor election might be used to deduct pre-group disallowed BIE carryforwards that would be limited under proposed § 1.163(j)–7(c)(3)(iv) (rules similar to the consolidated SRLY rules). Accordingly, the proposed regulations provide that a safe-harbor election cannot be made for a CFC group that has pre-group disallowed BIE carryforward. The Treasury Department and the IRS request comments on whether the safe-harbor election should be available for CFC groups with pre-group disallowed BIE carryforwards and, if so, appropriate methods of preventing pre-group disallowed BIE carryforwards that would be limited under proposed § 1.163(j)–7(c)(3)(iv) from being deductible by CFC group members of CFC groups that apply the safe-harbor election.

The Treasury Department and the IRS also request comments on appropriate modifications, if any, to the safe-harbor election that would further the goal of reducing the compliance burden on stand-alone applicable CFCs and CFC groups that would not have disallowed BIE if they applied the section 163(j) limitation.

9. Increase in Adjusted Taxable Income of U.S. Shareholders

As a general matter, a U.S. shareholder does not include in its ATI any portion of its specified deemed inclusions. Specified deemed inclusions include the U.S. shareholder's deemed income inclusions attributable to an applicable CFC and a non-excepted trade or business of the U.S. shareholder. See § 1.163(j)–1(b)(2)(ii)(G). Specified deemed inclusions also include amounts included in a domestic C corporation's allocable share of a domestic partnership's gross income inclusions under sections 951(a) and 951A(a) with respect to an applicable CFC that are investment income to the partnership, to the extent that such amounts are treated as properly allocable to a non-excepted trade or business of the domestic C corporation under §§ 1.163(j)–4(b)(3) and 1.163(j)–10.[7] However, consistent with comments received, proposed § 1.163(j)–7(j) allows a U.S. shareholder to include in its ATI a portion of its specified deemed inclusions that are attributable to either a stand-alone applicable CFC or a CFC group member, except to the extent attributable to section 78 ''gross-up'' inclusions. That portion is equal to the ratio of the applicable CFC's CFC excess taxable income over its ATI.

In the case of a stand-alone applicable CFC, CFC excess taxable income is equal to an amount that bears the same ratio to the applicable CFC's ATI as (i) the excess of 30 percent of the applicable CFC's ATI over the amount, if any, by which its BIE exceeds its BII and floor plan financing interest expense, bears to (ii) 30 percent of its ATI. In the case of a CFC group, each applicable CFC's CFC excess taxable income is determined by calculating the excess taxable income of the CFC group and allocating it to each CFC group member pro rata on the basis of the CFC group member's ATI. For any taxable year or specified period to which the 50 percent (rather than 30 percent) limitation applies under section 163(j)(10), the formula for calculating CFC excess taxable income is adjusted accordingly.

The Treasury Department and the IRS are concerned that taxpayers may inappropriately attempt to aggregate debt in certain specified group members for which a CFC group election is not in effect, thereby overleveraging some specified group members and artificially creating CFC excess taxable income in other specified group members for purposes of increasing the ATI of a U.S. shareholder.[8] Accordingly, the Treasury Department and the IRS have determined that any excess taxable income of a specified group member should not become available to increase the ATI of a U.S. shareholder unless a CFC group election is in effect and the CFC group has not exceeded its section 163(j) limitation. Accordingly, under proposed § 1.163(j)–7(j)(4)(ii), only U.S. shareholders of stand-alone applicable CFCs and CFC group members can increase their ATI for a portion of their specified deemed inclusion. To the extent that a CFC group election is not in effect, a U.S. shareholder may not increase its ATI for any portion of its specified deemed inclusion attributable to a specified group member of the specified group.

In addition, if a safe-harbor election is in effect with respect to the taxable year of a stand-alone applicable CFC or the specified period of a CFC group, CFC excess taxable income is not calculated for the stand-alone applicable CFC or the CFC group members. As a result, proposed § 1.163(j)–7(j)(4)(i) provides that a U.S. shareholder of a stand-alone applicable CFC or of a CFC group member for which the safe-harbor election is in effect does not increase its ATI for any portion of its specified deemed inclusion attributable to the stand-alone applicable CFC or CFC group member.

VI. Section 1.163(j)–8: Application of the Business Interest Deduction Limitation to Foreign Persons With Effectively Connected Income

A. Proposed § 1.163(j)–8 Contained in the 2018 Proposed Regulations

The 2018 Proposed Regulations under § 1.163(j)–8 provide rules for how section 163(j) applies to a nonresident alien individual or foreign corporation that is not an applicable CFC (specified foreign person) with ECI. Although the regulations under section 163(j) generally apply to specified foreign persons, a number of the general rules under section 163(j) need to be adjusted to take into account the fact that a specified foreign person is taxed only on its ECI rather than all of its income. Accordingly, the definitions for ATI, BIE, BII, and floor plan financing interest expense are modified to limit such amounts to items that are, or are allocable to, ECI. The 2018 Proposed Regulations also modify § 1.163(j)–10(c) to provide that a specified foreign person's interest expense and interest income are only allocable to excepted or non-excepted trades or businesses that have ECI.

Under the 2018 Proposed Regulations, a specified foreign person that is a partner in a partnership that has ECI (specified foreign partner) is required to modify the application of the general allocation rules in § 1.163(j)–6 with respect to ETI, EBIE, and EBII of the

[7] The Treasury Department and the IRS anticipate that a domestic partnership's gross income inclusions under sections 951(a) and 951A(a) will virtually always be investment income to the partnership. See section 163(j)(5), excluding ''investment interest'' subject to section 163(d) from the definition of business interest, and sections 163(d)(3)(A) and (d)(5), treating as investment interest any interest properly allocable to ''property which produces income of a type described in section 469(e)(1).'' See also § 1.469–2T(c)(3).

[8] For example, assume a U.S. shareholder wholly owns CFC1, which wholly owns CFC2. CFC1 and CFC2 each have $100x of ATI and no business interest income or floor plan financing interest expense. CFC1 and CFC2 have not made a CFC group election. If CFC1 and CFC2 each have $35x of business interest expense, under section 163(j), CFC1 and CFC2 could each deduct $30x of business interest expense and have a $5x disallowed business interest expense carryforward. Neither CFC1 nor CFC2 would have CFC excess taxable income. As a result, the U.S. shareholder would have no ATI inclusion from CFC1 or CFC2. However, if the CFCs move all of CFC2's debt to CFC1, CFC1 would deduct $30x of business interest expense and have a $40x disallowed business interest expense carryforward. Absent rules providing otherwise, CFC2 would have $100x of CFC excess taxable income and $100x of ATI, allowing the U.S. shareholder to include in its ATI its CFC income inclusion attributable to CFC2 (to the extent attributable to a non-excepted trade or business and not attributable to section 78 ''gross-up'' inclusions).

partnership to take into account only the partnership's items that are, or are allocable to, ECI. Although the section 163(j) limitation is determined on an entity basis by a partnership, the Treasury Department and the IRS determined that excess items of a partnership should only be used by the specified foreign partner to the extent that the excess items arise from partnership items that are ECI with respect to the specified foreign partner. The amount of ETI and EBIE to be used by a specified foreign partner was determined by multiplying the amount of the ETI or the EBIE allocated under § 1.163(j)–6 to the specified foreign partner by a fraction, the numerator of which is the ATI of the partnership, with the adjustments described previously to limit such amount to only items that are ECI, and the denominator of which is the ATI of the partnership determined under § 1.163(j)–6(d). The amount of EBII that could be used by a specified foreign partner was limited to the amount of allocable BII that is ECI from the partnership that exceeds allocable BIE that is allocable to income that is ECI from the partnership.

Lastly, the 2018 Proposed Regulations provide that an applicable CFC that has ECI must first apply the general rules of section 163(j) and the section 163(j) regulations to determine how section 163(j) applies to the applicable CFC. If the applicable CFC has disallowed BIE, the applicable CFC then must apportion a part of its disallowed BIE to BIE allocable to income that is ECI. The amount of disallowed BIE allocable to income that is ECI is equal to the disallowed BIE multiplied by a fraction, the numerator of which is the applicable CFC's ECI ATI, and the denominator of which is the CFC's ATI.

No comments were received on the 2018 Proposed Regulations under § 1.163(j)–8. Nonetheless, the Treasury Department and the IRS have become aware of certain distortions that can result under the 2018 Proposed Regulations. Accordingly, proposed § 1.163(j)–8 has been revised, and re-proposed, to alleviate these distortions and to provide additional guidance and clarity on the manner in which these rules apply to specified foreign partners and CFCs with ECI.

B. Proposed § 1.163(j)–8 in the Proposed Regulations

Proposed § 1.163(j)–8 in the Proposed Regulations (Proposed § 1.163(j)–8) provides rules concerning the application of section 163(j) to foreign persons with ECI.[9] Similar to proposed § 1.163(j)–8(b) in the 2018 Proposed Regulations, proposed § 1.163(j)–8(b)(1)–(5) provides that, for purposes of applying section 163(j) and the section 163(j) regulations to a specified foreign person, certain definitions (ATI, BIE, BII, and floor plan financing interest expense) are modified to take into account only ECI items. Additionally, proposed § 1.163(j)–8(b)(6) provides that, for purposes of applying § 1.163(j)–10(c) to a specified foreign person, only ECI items and assets that are U.S. assets are taken into account in determining the amount of interest income and interest expense allocable to a trade or business.

Proposed § 1.163(j)–8(c) determines the portion of a specified foreign partner's allocable share of ETI, EBIE, and EBII (as determined under § 1.163(j)–6) that is treated as ECI and the portion that is not treated as ECI. The portion of the specified foreign partner's allocable share of ETI that is ECI is equal to its allocable share of ETI multiplied by a fraction, the specified ATI ratio (which compares the specified foreign partner's distributive share of the partnership's ECI to its distributive share of the partnership's total income). The remainder of the specified foreign partner's allocable share of ETI is not ECI. See proposed § 1.163(j)–8(c)(1). Similar to ETI, the portion of the specified foreign partner's allocable share of EBII that is ECI is equal to its allocable share of EBII multiplied by a fraction, the specified BII ratio (which compares the specified foreign partner's allocable share of BII that is ECI to its allocable share of total BII). See proposed § 1.163(j)–8(c)(4).

The portion of the specified foreign partner's allocable share of EBIE that is ECI is determined by subtracting the portion of the specified foreign partner's allocable share of deductible BIE that is characterized as ECI from the amount of the specified foreign partner's allocable share of BIE that is characterized as ECI. See proposed § 1.163(j)–8(c)(2). A similar rule applies for purposes of determining the portion of EBIE that is not ECI. A specified foreign partner's allocable share of deductible BIE that is characterized as ECI or not ECI is determined by allocating the deductible BIE pro rata between the respective amounts of deductible BIE that the specified foreign partner would have if the specified foreign partner's allocable share of the ECI items of the partnership and the non-ECI items of the partnership were treated as separate partnerships and a 163(j) limitation was applied to each hypothetical partnership. However, no more deductible BIE can be characterized as ECI or not ECI than the specified foreign partner's allocable share of BIE that is ECI or the specified foreign partner's allocable share of BIE that is not ECI, respectively. Any deductible BIE in excess of the hypothetical partnership limitations is characterized as ECI or not ECI pro rata in proportion to the remaining amounts of the specified foreign partner's allocable share of BIE that is ECI and not ECI.

Proposed § 1.163(j)–8(d) determines the portion of deductible and disallowed BIE of a relevant foreign corporation (as defined in § 1.163(j)–1(b)(33)) that is characterized as ECI or not ECI. These rules are similar to the rules in proposed § 1.163(j)–8(c) for characterizing a specified foreign partner's allocable share of excess items of a partnership as ECI or not ECI in that they calculate the hypothetical section 163(j) limitation for two hypothetical foreign corporations—a foreign corporation with ECI and a foreign corporation with non-ECI—and allocate the deductible BIE between the two hypothetical limitations. The portion of the relevant foreign corporation's disallowed BIE that is ECI is determined by subtracting the portion of the relevant foreign corporation's deductible BIE that is characterized as ECI from the relevant foreign corporation's BIE that is ECI. A similar rule applies for purposes of determining the portion of disallowed BIE that is characterized as not ECI.

Proposed § 1.163(j)–8(e) provides rules regarding disallowed BIE. These rules provide that disallowed BIE is characterized as ECI or not ECI in the year in which it arises and retains its characterization in subsequent years. Additionally, an ordering rule determines the EBIE that is treated as paid or accrued by a specified foreign partner in a subsequent year. Specifically, the specified foreign partner's allocable share of EBIE is treated as paid or accrued by the specified foreign partner in a subsequent year pursuant to § 1.163(j)–6(g)(2)(i) in the order of the taxable years in which the allocable EBIE arose and pro rata between the specified foreign partner's allocable share of EBIE that is ECI and not ECI that arose in the same taxable year.

Proposed § 1.163(j)–8(e)(2) provides that, for purposes of characterizing deductible BIE and EBIE as ECI or not ECI, a specified foreign partner's BIE is

[9] For purposes of Proposed § 1.163(j)–8, the term *effectively connected income* (or *ECI*) means income or gain that is ECI, as defined in § 1.884–1(d)(1)(iii), and deduction or loss that is allocable to, ECI, as defined in § 1.884–1(d)(1)(iii).

deemed to include its allocable share of EBIE of partnerships in which it is a direct or indirect partner. As a result, EBIE of both top-tier partnerships and lower-tier partnerships is characterized as ECI or not ECI in the year in which it arises, even if it is not included in the specified foreign partner's allocable share of EBIE.

Proposed § 1.163(j)–8(f) provides rules coordinating the application of section 163(j) with § 1.882–5 and similar rules and with the branch profits tax. Proposed § 1.163(j)–8(f)(1)(i) provides that a foreign corporation first determines its interest expense on liabilities that are allocable to ECI under § 1.882–5 before applying section 163(j). Similarly, interest expense, as defined in § 1.163(j)–1(b)(23), that is not allocable to ECI under § 1.882–5 must be allocable to income that is ECI under the regulations under section 861 before section 163(j) is applied.

Proposed § 1.163(j)–8(f)(1)(ii) provides rules for determining the portion of a specified foreign partner's BIE that is ECI, as determined under § 1.882–5(b) through (d) or § 1.882–5(e) (§ 1.882–5 interest expense), that is treated as attributable to a partner's allocable share of interest expense of a partnership. As a general matter, the determination as to whether a partnership's items of income and expense are allocable to ECI is made by the partnership. However, the determination as to the amount of interest expense that is allocable to ECI is made by a partner, not the partnership. Because section 163(j) applies separately to partnerships and their partners, a determination must be made as to the source of § 1.882–5 interest expense. If the BIE is attributable to BIE of the partnership, it is subject to the rules of §§ 1.163(j)–6 and 1.163(j)–8(c).

The § 1.882–5 interest expense is first treated as attributable to interest expense on U.S. booked liabilities, determined under § 1.882–5(d)(2)(vii), of the partner or a partnership. Any remaining § 1.882–5 interest expense (excess § 1.882–5 interest expense) is treated as attributable to interest expense on liabilities of the partner in proportion to its U.S. assets (other than partnership interests) over all of its U.S. assets, and as attributable to interest expense on liabilities of the partner's direct or indirect partnership interests in proportion to the portion of the partnership interest that is a U.S. asset over all of the partner's U.S. assets. The total amount of § 1.882–5 interest expense attributed to the partner or a partnership (taking into account both interest expense on U.S. booked liabilities and excess § 1.882–5 interest expense) and interest expense on a liability described in § 1.882–5(a)(1)(ii)(A) or (B) (direct allocations) may never exceed the amount of the partner's interest expense on liabilities or the partner's allocable share of the partnership's interest expense on liabilities (the interest expense limitation). The interest expense limitation prevents more § 1.882–5 interest expense from being attributed to the partner or the partner's allocable share of interest expense of a partnership than the actual amount of such interest expense. Any excess § 1.882–5 interest expense that would have been attributed to the partner or a partnership, but for the interest expense limitation, is re-attributed in accordance with these attribution rules.

When excess § 1.882–5 interest expense has been attributed to all of the interest expense on liabilities of the foreign corporation and its allocable share of partnership interests that have U.S. assets, the remaining excess § 1.882–5 interest expense, if any, is first attributed to interest expense on liabilities of the foreign corporation (but not in excess of the interest expense limitation), and then, pro rata, to its allocable share of interest expense on liabilities of its partnership interests that do not have U.S. assets, subject to the interest expense limitation. See proposed § 1.163(j)–8(f)(1)(iii). These rules merely characterize interest expense of the foreign corporation and its partnership interests as ECI or not ECI. These rules do not change the amount of interest expense of the foreign corporation or its partnership interests.

The rule in proposed § 1.163(j)–8(f)(1) of 2018 Proposed Regulations providing that the disallowance and carryforwards of BIE does not affect effectively connected earnings and profits of a foreign corporation is not retained in Proposed § 1.163(j)–8. This rule is not necessary in Proposed § 1.163(j)–8 because the general rule regarding the effect of section 163(j) on earnings and profits in § 1.163(j)–4(c)(1) applies to effectively connected earnings and profits.

VII. Proposed § 1.469–9: Definition of Real Property Trade or Business

Section 469(c)(7)(C) defines real property trade or business by reference to eleven undefined terms. The Final Regulations amended § 1.469–9 to define two of the eleven terms—management and operations. In response to questions received about the application of section 469(c)(7)(C) to timberlands, these proposed regulations would provide definitions for two additional terms—development and redevelopment—to further clarify what constitutes a real property trade or business.

The Treasury Department and IRS have determined that real property development and redevelopment trades or businesses should be defined to include business activities that involve the preservation, maintenance, and improvement of forest-covered areas (timberland). Congress most likely intended and expected that such business activities would be excepted from section 163(j), through election, similar to other real property and farming businesses. However, because timber is specifically excluded from the definition of farming under other Code provisions (such as section 464(e)), the Treasury Department and IRS have determined that such business activities are more properly described by and should be included in the definition of real property trade or business for this purpose. These proposed regulations would clarify that ''real property development'' is the maintenance and improvement of raw land to make the land suitable for subdivision, further development, or construction of residential or commercial buildings, or to establish, cultivate, maintain or improve timberlands (generally defined as parcels of land covered by forest). Similarly, these proposed regulations would clarify that ''real property redevelopment'' is the demolition, deconstruction, separation, and removal of existing buildings, landscaping, and infrastructure on a parcel of land to return the land to a raw condition or otherwise prepare the land for new development or construction, or for the establishment and cultivation of new timberlands.

VIII. Proposed § 1.163(j)–2 and § 1.1256(e)–2: Section 1256 and Determination of Tax Shelter Status; Election To Use 2019 ATI To Determine 2020 Section 163(j) Limitation

A. Section 1256 and Determination of Tax Shelter Status

Several commenters raised questions regarding the exclusion of ''a tax shelter that is not permitted to use a cash method of accounting'' from the small business exemption provided in section 163(j)(3). Section 448 and § 1.448–1T describe limitations on the use of the cash method of accounting, including an explicit prohibition on the use of the cash method of accounting by a tax shelter. Section 448(d)(3) defines a tax shelter by cross reference to section 461(i)(3), which defines a tax shelter, in part, as a syndicate within the meaning of section 1256(e)(3)(B). Under § 1.448–1T(b)(3), a syndicate is defined as an entity that is not a C corporation if more than 35 percent of the losses of such entity during the taxable year are *allocated* to limited partners or limited entrepreneurs. Section 1256(e)(3)(B) refers instead to losses that are *allocable* to limited partners or limited entrepreneurs. As a result, the scope of the small business exemption in section 163(j)(3) is unclear. To provide clarity, and to make these rules consistent, the Treasury Department and the IRS would define the term syndicate for purposes of section 1256 using the actual allocation rule from the definition in § 1.448–1T(b)(3). This proposed definition is also consistent with the definition of a syndicate used in a number of private letter rulings that were issued under section 1256. See proposed § 1.1256(e)–2(a).

One commenter asked for clarification on how to compute the amount of losses to be allocated for purposes of determining syndicate status under section 1256(e)(3)(A). The commenter provided a particular fact pattern in which a small business would be caught in an iterative loop of (a) having net losses due to an interest deduction, (b) which would trigger disallowance of the exemption in section 163(j)(3), (c) which would trigger the application of section 163(j)(1) to reduce the amount of the interest deduction, (d) which would then lead to the taxpayer having no net losses and therefore being eligible for the application of section 163(j)(3). To address this fact pattern, the Treasury Department and the IRS have added rules providing that, for purposes of section 1256(e)(3)(B), losses are determined without regard to section 163(j). See proposed §§ 1.163(j)–2(d)(3) and 1.1256(e)–2(b).

Several commenters requested that the exemption in section 163(j)(3) be broadened to apply to all small businesses without regard to the parenthetical that denies the section 163(j)(3) exemption for a small business that is ‘‘a tax shelter that is not permitted to use a cash method of accounting.’’ See section 163(j)(3). One commenter specifically requested that, for a small business meeting the gross receipts test in section 448(c), all interests held by limited partners or limited entrepreneurs be treated as held by owners actively managing the business even if those interests would not qualify for the active management exception under section 1256(e)(3)(C). After considering the comments, the Treasury Department and the IRS have determined that the requests are contrary to both the statutory language in section 163(j)(3) and the accompanying legislative history and therefore decline to adopt the comments.

B. Election To Use 2019 ATI To Determine 2020 Section 163(j) Limitation

As stated in the Background section of this preamble, section 163(j)(10)(B)(i) allows a taxpayer to elect to use its 2019 ATI in determining the taxpayer's section 163(j) limitation for its taxable year beginning in 2020. Section 1.163(j)–2(b)(3) and (4) of the Final Regulations provide general rules regarding this election.

These proposed regulations clarify that, if the acquiring corporation in a transaction to which section 381 applies makes an election under section 163(j)(10)(B)(i), the acquiring corporation's 2019 ATI for purposes of section 163(j)(10)(B)(i) is its ATI for its last taxable year beginning in 2019 (subject to the limitation for short taxable years in section 163(j)(10)(B)(ii)). For example, assume that T's 2019 ATI is $100 and A's 2019 ATI is $200. If T merges into A during A's 2020 taxable year in a transaction described in section 368(a)(1)(A), and if A makes an election under section 163(j)(10)(B)(i), A's 2019 ATI for purposes of this election is $200. Similarly, these proposed regulations clarify that a consolidated group's 2019 ATI for purposes of section 163(j)(10)(B)(i) is the consolidated group's ATI for its last taxable year beginning in 2019 (subject to the limitation in section 163(j)(10)(B)(ii)). The Treasury Department and the IRS request comments on these proposed rules. The Treasury Department and the IRS also request comments on (1) whether the 2019 ATI of an acquired corporation in a transaction to which section 381 applies should be included in the acquiring corporation's 2019 ATI for purposes of section 163(j)(10)(B)(i) and (2) how such a rule would address more complex fact patterns, such as situations where the acquiring corporation is acquired in a subsequent transaction described in section 381, or where the acquired corporation and the acquiring corporation have different tax years.

IX. Proposed § 1.163(j)–10: Application of Corporate Look-Through Rules to Tiered Structures

For purposes of determining the extent to which a shareholder's basis in the stock of a domestic non-consolidated C corporation or CFC is allocable to an excepted or non-excepted trade or business, § 1.163(j)–10(c)(5)(ii)(B) provides several look-through rules whereby the shareholder ‘‘looks through’’ to the corporation's basis in its assets.

A commenter pointed out that the application of these look-through rules may produce distortive results in certain situations. For example, assume Corporation X's basis in its assets is split equally between X's excepted and non-excepted trades or businesses, and that (as a result) X has a 50 percent exempt percentage applied to its interest expense. However, rather than operate its excepted trade or business directly, X operates its excepted trade or business through a wholly owned, non-consolidated subsidiary (Corporation Y), and each of X and Y borrows funds from external lenders. Assuming for purposes of this example that neither the anti-avoidance rule in § 1.163(j)–2(h) nor the anti-abuse rule in § 1.163(j)–10(c)(8) applies, Y's interest expense would not be subject to the section 163(j) limitation because Y is engaged solely in an excepted trade or business. Moreover, a portion of X's interest expense also would be allocable to an excepted trade or business by virtue of the application of the look-through rule in proposed § 1.163(j)–10(c)(5)(ii)(B)(2) to X's basis in Y's stock.

The anti-avoidance rule in proposed § 1.163(j)–2(h) and the anti-abuse rule in proposed § 1.163(j)–10(c)(8) would preclude the foregoing result in certain circumstances. However, these proposed regulations would modify the look-through rule for domestic non-consolidated C corporations and CFCs to limit the potentially distortive effect of this look-through rule on tiered structures in situations to which the anti-avoidance and anti-abuse rules do not apply. More specifically, these proposed regulations would modify the look-through rule for non-consolidated C corporations to provide that, for purposes of determining a taxpayer's basis in its assets used in excepted and non-excepted trades or businesses, any such corporation whose stock is being looked through may not itself apply the look-through rule.

For example, P wholly and directly owns S1, which wholly and directly owns S2. Each of these entities is a non-consolidated C corporation to which the small business exemption does not apply. In determining the extent to which its interest expense is subject to the section 163(j) limitation, S1 may look through the stock of S2 for purposes of allocating S1's basis in its S2 stock between excepted and non-excepted trades or businesses. However, in determining the extent to which P's interest expense is subject to the section 163(j) limitation, S1 may not look through the stock of S2 for purposes of allocating P's basis in its S1 stock between excepted and non-excepted trades or businesses.

However, the Treasury Department and the IRS are aware that taxpayers are organized into multi-tiered structures for legitimate, non-tax reasons. The Treasury Department and the IRS request comments on the proposed limitation on the application of the corporate look-through rules. The Treasury Department and the IRS also request comments on whether there are other situations in which the look-through rules for domestic non-consolidated C corporations or CFCs should apply and whether there are other approaches for addressing the distortions that these proposed rules are intended to minimize.

Proposed Applicability Dates

These Proposed Regulations are proposed to apply to taxable years beginning on or after 60 days after the date the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**.

Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may rely on § 1.163–14, § 1.163–15, § 1.163(j)–2(d)(3), or § 1.1256(e)–2 of these Proposed Regulations for a taxable year beginning after December 31, 2017, and before 60 days after the date the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**, provided taxpayers and their related parties consistently follow all of the rules of the relevant section of the Proposed Regulations for that taxable year and for each subsequent taxable year. Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply § 1.163–14, 1.163–15, 1.163(j)–2(d)(3), or 1.1256(e)–2 of the final version of these Proposed Regulations for a taxable year beginning after December 31, 2017, and before 60 days after the date the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**, provided that taxpayers and their related parties consistently apply all of the rules of the relevant section, as applicable, to that taxable year and each subsequent taxable year. See also §§ 1.163–14(i), 1.163–15(b), 1.163(j)–2(k)(2), and 1.1256(e)–2(d) of these Proposed Regulations.

Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), who apply the Final Regulations (as defined in the Explanation of Provisions) published elsewhere in this issue of the **Federal Register** to a taxable year beginning after December 31, 2017, and before 60 days after the Treasury Decision adopting these rules as final regulations is published in the **Federal Register** may rely on §§ 1.163(j)–1(b)(1)(iv)(B) and 1.163(j)–1(b)(1)(iv)(E) of these Proposed Regulations for a taxable year beginning after December 31, 2017, and before 60 days after the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**, provided that taxpayers and their related parties consistently apply the rules of both §§ 1.163(j)–1(b)(1)(iv)(B) and 1.163(j)–1(b)(1)(iv)(E) of these Proposed Regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year and each subsequent taxable year See also § 1.163(j)–1(c)(4)(i) of these Proposed Regulations.

Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), who apply the Final Regulations published elsewhere in this issue of the **Federal Register** to a taxable year beginning after December 31, 2017, and before 60 days after the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**, may rely on the rules in § 1.163(j)–2(b)(3)(iii) and (iv) of these Proposed Regulations for such taxable year, provided that taxpayers and their related parties consistently follow the rules of both § 1.163(j)–2(b)(3)(iii) and (iv) for that taxable year and for each subsequent taxable year beginning before 60 days after the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**. Taxpayers not applying the Final Regulations to taxable years beginning before November 13, 2020 may not rely on the rules in § 1.163(j)–2(b)(3)(iii) and (iv) of these Proposed Regulations for those taxable years. See also § 1.163(j)–2(k)(2) of these Proposed Regulations.

Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b), who apply the Final Regulations published elsewhere in this issue of the **Federal Register** to a taxable year beginning after December 31, 2017, and before 60 days after the Treasury Decision adopting these rules as final regulations is published in the **Federal Register** may rely on the rules in § 1.163(j)–10(c)(5)(ii)(D)(2), 1.469–4(d)(6), or 1.469–9(b)(2) of these Proposed Regulations for a taxable year beginning after December 31, 2017, and before 60 days after the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**, provided that taxpayers and their related parties consistently follow the rules of § 1.163(j)–10(c)(5)(ii)(D)(2), 1.469–4(d)(6), or 1.469–9(b)(2) of these Proposed Regulations, as applicable, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–4, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, for that taxable year and for each subsequent taxable year. See also §§ 1.163(j)–10(f)(2) and 1.469–11(a)(1) and (4) of these Proposed Regulations.

Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b), may rely on the rules in § 1.163(j)–6 of these Proposed Regulations for a taxable year beginning after December 31, 2017, and before 60 days after the Treasury Decision adopting these rules as final regulations is published in the **Federal Register**, provided that taxpayers and their related parties also apply the rules of § 1.163(j)–6 in the Final Regulations and consistently follow all of those rules for that taxable year and for each subsequent taxable year. See also § 1.163(j)–6(p)(2) of these Proposed Regulations.

Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), who apply the Final Regulations published elsewhere in this issue of the **Federal Register** to a taxable year beginning after December 31, 2017, and before 60 days after the date the Final Regulations are published in the **Federal Register**, may rely on §§ 1.163(j)–7 and 1.163(j)–8 of these Proposed Regulations for that taxable year, provided the taxpayers and their related parties also rely on §§ 1.163(j)–7 and 1.163(j)–8 of these Proposed Regulations and apply the Final Regulations for each subsequent taxable year. Taxpayers who choose not to apply the Final Regulations to a taxable year beginning after December 31, 2017, and before 60 days after the date the Final Regulations are published in the **Federal Register** may not rely on either § 1.163(j)–7 or 1.163(j)–8 of these Proposed Regulations for that taxable year. For any taxable year beginning on or after 60 days after the date the Final Regulations are published in the

Federal Register and before 60 days after the date the Treasury Decision adopting these Proposed Regulations as final regulations is published in the **Federal Register**, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may rely on §§ 1.163(j)–7 and 1.163(j)–8 of these Proposed Regulations provided they consistently follow all of the rules of §§ 1.163(j)–7 and 1.163(j)–8 for such taxable year and for each subsequent taxable year beginning before 60 days after the Treasury Decision adopting these Proposed Regulations as final regulations is published in the **Federal Register**. See also §§ 1.163(j)–7(m) and 1.163(j)–8(j) of these Proposed Regulations. Taxpayers and their related parties who rely on § 1.163(j)–7 of these Proposed Regulations for any taxable year ending before November 13, 2020 can make a CFC group election or a safe-harbor election even if the deadline provided in § 1.163(j)–7(e)(5)(iii) or (h)(5)(i) of these Proposed Regulations has passed. Such taxpayers and their related parties are permitted to make the election on an amended Federal income tax return filed on or before the due date (taking into account extensions, if any) of the original Federal income tax return for the first taxable year ending after November 13, 2020.

See part III.B of the Explanation of Provisions for rules concerning reliance on these Proposed Regulations with respect to section 163(j) interest dividends.

Special Analyses

I. Regulatory Planning and Review—Economic Analysis

Executive Orders 13771, 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, reducing costs, harmonizing rules, and promoting flexibility. The Executive Order 13771 designation for any final rule resulting from these proposed regulations will be informed by comments received. The preliminary Executive Order 13771 designation for this proposed rule is regulatory.

These proposed regulations have been designated by the Office of Information and Regulatory Affairs as subject to review under Executive Order 12866 pursuant to the Memorandum of Agreement (MOA, April 11, 2018) between the Treasury Department and the Office of Management and Budget (OMB) regarding review of tax regulations. OMB has designated the proposed regulations as economically significant under section 1(c) of the MOA. Accordingly, the proposed regulations have been reviewed by OMB's Office of Information and Regulatory Affairs.

A. Background and Need for These Proposed Regulations

Section 163(j), substantially revised by the Tax Cuts and Jobs Act (TCJA), provides a set of relatively complex statutory rules that impose a limitation on the amount of business interest expense that a taxpayer may deduct for Federal tax purposes. This limitation does not apply to businesses with gross receipts of $25 million or less (inflation adjusted). This provision has the general effect of putting debt-financed investment by businesses on a more equal footing with equity-financed investment, a treatment that Congress believed will lead to a more efficient capital structure for firms. See Senate Budget Explanation of the Bill as Passed by SFC (2017–11–20) at pp. 163–4.

As described in the Background section earlier, the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) amended section 163(j) to provide special rules relating to the adjusted taxable income (ATI) limitation for taxable years beginning in 2019 or 2020.

Because this limitation on deduction for business interest expense is new, taxpayers would benefit from regulations that explain key terms and calculations. The Treasury Department and the IRS published proposed regulations in December 2018 (2018 Proposed Regulations) and are issuing final regulations simultaneously with the current proposed regulations. This current set of proposed regulations covers topics that were reserved in the 2018 Proposed Regulations, were raised by commenters to the proposed regulations, or need to be re-proposed.

B. Overview of the Proposed Regulations

The proposed regulations provide guidance on the definition of interest as it relates to income flowing through regulated investment companies (RICs); debt-financed distributions from pass-through entities; the treatment of business interest expense for publicly traded partnerships and trading partnerships [10]; the application of the section 163(j) limitation in the context of self-charged interest; and the treatment of excess business interest expense in tiered-partnership structures. The proposed regulations also modify the definition of real property development and real property redevelopment in section 1.469–9 of the regulations and the definition of syndicate for purposes of applying the small business exception in section 163(j)(3). The proposed regulations also re-propose rules regarding the application of the interest limitation to foreign corporations (including controlled foreign corporations as defined in section 957(a)) and United States shareholders of controlled foreign corporations, and the applicability of the section 163(j) limitation to foreign persons with U.S. effectively connected income.

C. Economic Analysis

1. Baseline

The Treasury Department and the IRS have assessed the benefits and costs of these proposed regulations relative to a no-action baseline that reflects anticipated Federal income tax-related behavior in the absence of these regulations.

2. Summary of Economic Effects

The proposed regulations provide certainty and clarity to taxpayers regarding terms and calculations that are contained in section 163(j), which was substantially modified by TCJA. In the absence of this clarity, the likelihood that different taxpayers would interpret the rules regarding the deductibility of business interest expense differently would be exacerbated. In general, overall economic performance is enhanced when businesses face more uniform signals about tax treatment. Certainty and clarity over tax treatment also reduce compliance costs for taxpayers.

For those situations where taxpayers would generally adopt similar interpretations of the statute even in the absence of guidance, the proposed regulations provide value by helping to ensure that those interpretations are consistent with the intent and purpose of the statute. For example, the proposed regulations may specify a tax treatment that few or no taxpayers would adopt in the absence of specific guidance.

The Treasury Department and the IRS project that the proposed regulations

[10] A trading partnership is a partnership engaged in the per se non-passive activity of trading personal property (including market securities) for the account of owners of interests in the activity, as described in section 1.469–1T(e)(6) (trading partnerships).

will have an annual economic effect greater than $100 million ($2019). This determination is based on the substantial volume of business interest payments in the economy [11] and the general responsiveness of business investment to effective tax rates,[12] one component of which is the deductibility of interest expense. Based on these two magnitudes, even modest changes in the deductibility of interest payments (and in the certainty of that deductibility) provided by the proposed regulations, relative to the no-action baseline, can be expected to have annual effects greater than $100 million. This claim is particularly likely to hold for the first set of general section 163(j) guidance that is promulgated following major legislation, such as TCJA, and for other major guidance, which we have determined includes these proposed regulations.

Regarding the nature of the economic effects, the Treasury Department and the IRS project that the proposed regulations will increase investment in the United States and increase the proportion that is debt-financed, relative to the no-action baseline. We have further determined that these effects are consistent with the intent and purpose of the statute. Because taxpayer favorable provisions will lead to a decrease in Federal tax revenue relative to the no-action baseline, there may be an increase in the Federal deficit relative to the no-action baseline. This may lead to a decrease in investment by taxpayers not directly affected by these proposed regulations, relative to the no-action baseline. This effect should be weighed against the enhanced efficiency arising from the clarity and enhanced consistency with the intent and purpose of the statute provided by these regulations. The Treasury Department and the IRS have determined that the proposed regulations provide a net benefit to the U.S. economy.

The Treasury Department and the IRS have not undertaken more precise quantitative estimates of these effects because many of the definitions and calculations under 163(j) are new and many of the economic decisions that are implicated by these proposed regulations involve highly specific taxpayer circumstances. We do not have readily available data or models to estimate with reasonable precision the types and volume of different financing arrangements that taxpayers might undertake under the proposed regulations versus the no-action baseline.

In the absence of such quantitative estimates, the Treasury Department and the IRS have undertaken a qualitative analysis of the economic effects of the proposed regulations relative to the no-action baseline and relative to alternative regulatory approaches. This analysis is presented in Part I.C.3 of this Special Analyses.

The Treasury Department and the IRS solicit comments on these findings and more generally on the economic effects of these proposed regulations. The Treasury Department and the IRS particularly solicit data, other evidence, or models that could be used to enhance the rigor of the process by which the final regulations might be developed.

3. Economic Effects of Specific Provisions

a. Definition of Interest

The final regulations set forth several categories of amounts and transactions that generate interest for purposes of section 163(j). The proposed regulations provide further guidance on the definition of interest relevant to the calculation of interest expense and interest income. In particular, the proposed regulations provide rules under which the dividends paid by a RIC that earns net business interest income (referred to as section 163(j) interest dividends) are to be treated as interest income by the RIC's shareholders. That is, under the proposed regulations, certain interest income earned by the RIC and paid to a shareholder as a dividend is treated as if the shareholder earned the interest income directly for purposes of section 163(j).

To the extent that taxpayers believed, in the absence of the proposed regulations, that dividends paid by RICs are not treated as business interest income for the purposes of the section 163(j) limitation, then taxpayers will likely respond to the proposed regulations by reducing their holding of other debt instruments and increasing investment in RICs. The Treasury Department and the IRS have determined that this treatment is consistent with the intent and purpose of the statute.

Number of Affected Taxpayers. The Treasury Department and the IRS have determined that the rules regarding section 163(j) interest dividends will potentially affect approximately 10,000 RICs. The Treasury Department and the IRS do not have readily available data on the number of RIC shareholders that would receive section 163(j) interest dividends that the shareholder could treat as business interest income for purposes of the shareholder's section 163(j) limitation.

b. Provisions Related to Partnerships

i. Trading Partnerships

Section 163(j) limits the deductibility of interest expense at the partnership level. These proposed regulations address commenter concerns about the interaction between this section 163(j) limitation and the section 163(d) partner level limitation on interest expense that existed prior to TJCA. Under logic described in the preamble to the 2018 Proposed Regulations, section 163(j) limitations would apply at the partnership level while section 163(d) limitations would apply at the partner level and these tests would be applied independently. Commenters suggested and Treasury has agreed that the correct interpretation of the statute is to exempt interest expense that is limited at the partner level by section 163(d) from the partnership level section 163(j) limitation in accordance with the language of section 163(j)(5).

These proposed regulations provide that interest expense at the partnership level that is allocated to non-materially participating partners subject to section 163(d) is not included in the section 163(j) limitation calculation of the partnership. Generally, the section 163(d) limitation is more generous than the section 163(j) limitation. Relative to the 2018 Proposed Regulations, this change may encourage these partners to incur additional interest expense because they will be less likely to be limited in their ability to use it to offset other income. Commenters argued that exempting from section 163(j) any interest expense allocated to non-materially participating partners subject to section 163(d) will treat this interest expense in the same way as the interest expense generated through separately managed accounts, which are not subject to section 163(j) limitations.

The Treasury Department and the IRS project that these proposed regulations will result in additional investment in trading partnerships and generally higher levels of debt in any given trading partnership relative to the 2018 Proposed Regulations. Because investments in trading partnerships may be viewed as economically similar to investments in separately managed accounts arrangements, we further project that the proposed regulations, by making the tax treatments of these two arrangements generally similar, will

[11] Interest deductions in tax year 2013 for corporations, partnerships, and sole proprietorships were approximately $800 billion.

[12] See E. Zwick and J. Mahon, ''Tax Policy and Heterogeneous Investment Behavior,'' at *American Economic Review* 2017, 107(1): 217–48 and articles cited therein.

improve U.S. economic performance relative to the no-action baseline.

Number of Affected Taxpayers. The Treasury Department and the IRS have determined that the rules regarding trading partnerships will potentially affect approximately 275,000 taxpayers. This number was reached by determining, using data for the 2017 taxable year, the number of Form 1065 and Form 1065–B filers that (1) completed Schedule B to Form 1065 and marked box b, c, or d in question 1 to denote limited partnership, limited liability company, or limited liability partnership status; and (2) have a North American Industry Classification System (NAICS) code starting with 5231 (securities and commodity contracts intermediation and brokerage), 5232 (securities and commodity exchanges), 5239 (other financial investment activities), or 5259 (other investment pools and funds).

Additionally, the Treasury Department and the IRS have determined that the rules regarding publicly traded partnerships will potentially affect approximately 80 taxpayers. This number was reached by determining, using data for the 2017 taxable year, the number of Form 1065 and 1065–B filers with gross receipts exceeding $25 million that answered ''yes'' to question 5 on Schedule B to Form 1065 denoting that the entity is a publicly traded partnership. The Treasury Department and the IRS do not have readily available data on the number of filers that are tax shelters that are potentially affected by these provisions.

ii. Debt-Financed Distributions

Prior to TCJA, partners were responsible for determining the applicability of any limitations on the use of proceeds from debt because limitations on interest expense deductibility were determined at the partner level. Under section 163(j) as amended by TCJA, the partnership is required to complete a calculation to determine its limitation on trade or business interest expense. These proposed regulations provide guidance on the method that partnerships and partners should use to allocate interest expense in cases where a partner receives a distribution financed from debt. The Treasury Department and the IRS project that this guidance will reduce taxpayer uncertainty regarding the application of section 163(j) in this situation relative to the no-action baseline.

The proposed regulations require that partnerships allocate the interest expense of the partners not receiving a debt-financed distribution first. This interest expense is allocated to trade or business expense to the extent of the partnership's expenses. The character of any remaining interest expense is determined based on the partnership's asset basis. Next, the proposed regulations allocate the interest expense of the partner receiving the debt-financed distribution. If there is any remaining business expense that was not used by the other partners it is used first to allocate the interest expense. Then the partner receiving the debt financed distribution looks to the use of the proceeds of the distribution to determine the character of any additional interest expense.

This procedure provides lower compliance costs relative to alternative regulatory approaches. Any alternative method that required information on the partner's use of the proceeds to determine the partnership level section 163(j) limitation would have increased compliance costs for partnerships and partners because it would require a new reporting from partners to partnerships. In cases of tiered partnerships, this reporting could become extremely complex. The method outlined in these proposed regulations avoids the need for partnerships and other partners to have information about the use the debt-financed distribution proceeds. However, it maintains that interest expense allocated to the partner receiving the debt-financed distribution could still be subject to other limitations besides section 163(j) based on the use of the proceeds. For example, proceeds used for personal expenditures would still be subject to section 163(h) limitations on interest expense, which may be seen as an important existing anti-abuse provision.

The proposed procedure bases the allocation rules on optional and general allocation rules outlined in a previously issued notice, Notice 89–35, which will minimize compliance costs to partnerships (relative to the no-action baseline) to the extent that they are already familiar with allocating interest expense first to the partnership's business expenses and subsequently based on assets. Relative to the no-action baseline, the Treasury Department and the IRS expect these proposed regulations will reduce taxpayer uncertainty regarding the application of section 163(j). Treasury and IRS expect that this resolution of uncertainty itself will reduce taxpayer compliance costs and encourage similarly situated taxpayers to interpret section 163(j) similarly.

Number of Affected Taxpayers. The Treasury Department and the IRS are not currently able to determine the number of taxpayers affected by rules regarding debt financed distributions because debt financed distributions are not separately identified on tax forms, and therefore using the numbers of entities reporting interest on a Form K–1, Schedule C or Schedule E would produce overly broad results.

iii. Tiered Partnerships

Section 163(j) does not explicitly address how the interest deduction limitation should be applied to tiered partnerships. The 2018 Proposed Regulations requested comments on the treatment of tiered partnership structures. Suppose that an upper-tier partnership (UTP) is a partner of a lower-tier partnership (LTP), and that the LTP has business interest expense that is limited under section 163(j). Under the 2018 Proposed Regulations, the UTP would receive an excess business interest expense (EBIE) carryforward from the LTP. In response to comments received, these proposed regulations adopt the Entity Approach and specify that this EBIE carryforward should not be allocated to the partners of the UTP for purposes of section 163(j).

While some commenters favored the Entity Approach that these proposed regulations adopt, others favored an alternative under which the EBIE carryforward would be allocated to the UTP's partners (Aggregate Approach). Additionally, if the UTP's partner were itself a partnership, the EBIE would again be allocated to that partnership's partners. This would continue until the EBIE is eventually allocated to a non-partnership partner. Relative to the Entity Approach, the Aggregate Approach generally places greater compliance burden on partners. Under the Aggregate Approach, partners would be required to keep records linking separate amounts of EBIE to the partnerships that generated them. In simple partnership structures, this is not onerous; however, in a partnership structure with many tiers and many partners, this would prove cumbersome. In contrast, under the Entity Approach, only the UTP keeps a record of the EBIE carryforward.

In summary, the Treasury Department and the IRS project lower record-keeping requirements, higher compliance rates, and easier compliance monitoring of tiered partnerships under the Entity Approach relative to the Aggregate Approach, with no meaningful difference in the economic decisions that taxpayers would make under the two approaches.

Moreover, relative to the no-action baseline, the Treasury Department and the IRS expect these proposed regulations for tiered partnerships will reduce taxpayer uncertainty regarding the application of section 163(j). Treasury and IRS expect that this resolution of uncertainty itself will reduce taxpayer compliance costs and encourage similarly situated taxpayers to interpret section 163(j) similarly.

iv. Self-Charged Lending

The 2018 Proposed Regulations requested comments on the treatment of lending transactions between a partnership and a partner (self-charged lending transactions). Suppose that a partnership receives a loan from a partner and allocates the resulting interest expense to that partner. Prior to the TCJA, the interest income and interest expense from this loan would net precisely to zero on the lending partner's tax return. Under section 163(j) as revised by TCJA, however, the partnership's interest expense deduction may now be limited. Therefore, in absence of specific regulatory guidance, the lending partner may receive interest income from the partnership accompanied by less-than-fully-offsetting interest expense. Instead, the lending partner would receive EBIE, which would not be available to offset his personal interest income. This outcome has the effect of increasing the cost of lending transactions between partners and their partnerships relative to otherwise similar financing arrangements.

To avoid this outcome, these proposed regulations treat the lending partner's interest income from the loan as excess business interest income (EBII) from the partnership, but only to the extent of the partner's share of any EBIE from the partnership for the taxable year. This allows the interest income from the loan to be offset by the EBIE. The business interest expense (BIE) of the partnership attributable to the lending transaction will thus be treated as BIE of the partnership for purposes of applying section 163(j) to the partnership.

The Treasury Department and the IRS expect that these proposed regulations will lead a higher proportion of self-charged lending transactions in partnership financing, relative to the no-action baseline. We further project that these proposed regulations will increase the proportion of partnership financing that is debt-financed relative to the no-action baseline. We have determined that these effects are consistent with the intent and purpose of the statute.

Number of Affected Taxpayers. The Treasury Department and the IRS do not have readily available data to determine the number of taxpayers affected by rules regarding self-charged interest because no reporting modules currently connect these payments by and from partnerships.

c. Provisions Related to Controlled Foreign Corporations (CFCs)

i. How To Apply Section 163(j) When CFCs Have Shared Ownership

The Final Regulations clarify that section 163(j) and the section 163(j) regulations apply to determine the deductibility of a CFC's business interest expense for tax purposes in the same manner as these provisions apply to a domestic corporation. These proposed regulations provide further rules and guidance on how section 163(j) applies to CFCs when CFCs have shared ownership and are eligible to be members of CFC groups.

The Treasury Department and the IRS considered three options with respect to the application of section 163(j) to CFC groups. The first option was to apply the 163(j) limitation to CFCs on an individual basis, regardless of whether CFCs have shared ownership. However, if section 163(j) is applied on an individual basis, business interest deductions of individual CFCs may be limited by section 163(j) even when, if calculated on a group basis, business interest deductions would not be limited. Taxpayers could restructure or ''self-help'' to mitigate the effects of the section 163(j) limitation, but that option involves economically restructuring costs for the taxpayer (relative to the third option, described subsequently) with no corresponding economically productive activity.

The second option, which was proposed in the 2018 Proposed Regulations, was to allow an election to treat related CFCs and their U.S. shareholders as a group. Under this option, while the section 163(j) rules would still be computed at the individual CFC level, the ''excess taxable income'' of a CFC could be passed up from lower-tier CFCs to upper-tier CFCs and U.S. shareholders in the same group. Excess taxable income is the amount of income by which a CFC's adjusted taxable income (ATI) exceeds the threshold amount of ATI below which there would be disallowed business expense.

Many comments suggested that computing a section 163(j) limitation for each CFC and rolling up CFC excess taxable income would be burdensome for taxpayers, especially since some multinational organizations have hundreds of CFCs. In addition, comments noted that the ability to pass up excess taxable income would encourage multinational organizations to restructure such that CFCs with low interest payments and high ATI are lower down the ownership chain and CFCs with high interest payments and low ATI are higher up in the chain of ownership. Similar to the first option, this restructuring would be expensive to taxpayers without any corresponding productive economic activity.

The third option was to allow taxpayers to elect to apply the section 163(j) rules to CFC groups on an aggregate basis, similar to the rules applicable to U.S. consolidated groups. This option was suggested by many comments and is the approach taken in the proposed regulations. Under this option, a single 163(j) limitation is computed for a CFC group by summing the items necessary for this computation (*e.g.,* current-year business interest expense and ATI) across all CFC group members. The CFC group's limitation is then allocated to each CFC member using allocation rules similar to those that apply to U.S. consolidated groups.

This option reduces the compliance burden on taxpayers in comparison to applying the section 163(j) rules on an individual CFC basis and calculating the excess taxable income to be passed up from lower tier CFCs to higher tier CFCs. In comparison to the first and second options, this option also removes the incentive for taxpayers to undertake costly restructuring, since the location of interest payments and ATI among CFC group members will not affect the interest disallowance for the group.

The proposed regulations also set out a number of rules to govern membership in a CFC group. These rules specify which CFCs can be members of the same CFC group, how CFCs with U.S. effectively connected income (ECI) should be treated, and the timing for making or revoking a CFC group election. These rules provide clarity and certainty to taxpayers regarding the CFC group election for section 163(j). In the absence of these regulations, taxpayers would face uncertainty regarding CFC group membership, and may make financing decisions or undertake restructuring that would be inefficient relative to the proposed regulations.

Number of Affected Taxpayers. The population affected by this proposed rule includes any taxpayer with ownership in a CFC group, consisting of two or more CFCs that has average gross receipts over a three year period in excess of $25 million. The Treasury

Department and the IRS estimate that there are approximately 7,500 taxpayers with two or more CFCs based on counts of e-filed tax returns for tax years 2015–2017. This estimate includes C corporations, S corporations, partnerships, and individuals with CFC ownership.

ii. CFC Excess Taxable Income and ATI of U.S. Shareholders

Generally, for the purposes of computing interest expense disallowed under section 163(j), deemed income inclusions, such as subpart F and GILTI inclusions, are excluded from a U.S. shareholder's ATI under the Final Regulations. The proposed regulations allow a U.S. shareholder to add back to its ATI a percentage of its deemed income inclusions attributable to an applicable CFC. That percentage is equal to the ratio of the CFC's excess taxable income to its ATI.

The Treasury Department and the IRS considered three options with respect to the addition of deemed income inclusions to a U.S. shareholder's ATI. The first option is to allow such inclusions to be added to ATI with respect to any of a taxpayer's applicable CFCs regardless of whether a CFC group election is made. However, under this option, taxpayers with a number of highly leveraged CFCs would have the incentive to not make a CFC group election and concentrate debt in certain CFCs. The taxpayer could thereby reduce the leverage of other CFCs in order to create excess taxable income in those CFCs. This excess taxable income could be then passed up to increase the U.S. shareholder's ATI. This incentive could lead to costly debt shifting among CFCs with no corresponding productive economic activity.

The second option considered was to allow such income inclusions to be added to ATI with respect to CFC group members only. Deemed income attributable to CFCs that are not members of groups would not be allowed to be added to a U.S. shareholder's ATI. This would remove the incentive for taxpayers to aggregate debt in certain CFCs, since if CFCs are treated as members of a group, then the distribution of interest payments across members will not affect the total excess taxable income of the group. However, comments noted that this option would not allow deemed income from stand-alone CFCs, which do not meet the requirements to join a CFC group, to increase shareholders' ATI.

The third option, which is proposed by the Treasury Department and the IRS, is to allow such income inclusions to be added to ATI with respect to both CFC group members and stand-alone CFCs. Under this option, if CFCs are eligible to be members of a CFC group, then the group election must be made in order for deemed inclusions attributable to these CFCs to increase shareholder ATI. The ATI of a U.S. shareholder can also be increased with respect to CFCs that are not eligible to be members of CFC groups. In this way, the rule does not penalize, relative to shareholders of CFC groups, shareholders which own only one CFC or own CFCs which for other reasons are not eligible for group membership.

Number of Affected Taxpayers. The population of affected taxpayers includes any taxpayer with a CFC since the proposed rule affects both stand-alone CFCs as well as CFC groups. The Treasury Department and the IRS estimate that there are approximately 10,000 to 11,000 affected taxpayers based on a count of e-filed tax returns for tax years 2015–2017. These counts include C corporations, S corporations, partnerships, and individuals with CFC ownership that meet a $25 million three-year average gross receipts threshold. The Treasury Department and the IRS do not have readily available data on the number of filers that are tax shelters that are potentially affected by these provisions.

d. Election To Use 2019 ATI To Determine 2020 Section 163(j) Limitation for Consolidated Groups

The proposed regulations provide that if a taxpayer filing as a consolidated group elects to substitute its 2019 ATI for its 2020 ATI, that group can use the consolidated group ATI for the 2019 taxable year, even if membership of the consolidated group changed in the 2020 taxable year. For example, suppose consolidated group C has three members in the 2019 taxable year, P, the common parent of the consolidated group, and S1 and S2, which are both wholly owned by P. In the 2019 taxable year, each member of consolidated group C had $100 of ATI on a stand-alone basis, for a total of $300 of ATI for the consolidated group C. In the 2020 taxable year, consolidated group C sells all of the stock of S2 and acquires all of the stock of a new member, S3. In the 2019 taxable year, S3 had $50 in ATI on a stand-alone basis. Under the proposed regulations, consolidated group C may elect to use $300 in ATI from 2019 as a substitute for its ATI in the 2020 taxable year.

The Treasury Department and the IRS considered as an alternative basing the 2019 ATI on the membership of the consolidated group in the 2020 taxable year. In the example in the previous paragraph, this approach would subtract out the $100 in ATI from S2 and add the $50 in ATI from S3, for a total of $250 in 2019 ATI that could potentially be substituted for 2020 ATI for consolidated group C. This approach would add burden to taxpayers relative to the proposed regulations by requiring additional calculations and tracking of ATI on a member-by-member basis to determine the amount of 2019 ATI that can be used in the 2020 taxable year without providing any general economic benefit.

In addition, the 2019 tax year will have closed for many taxpayers by the time these proposed regulations will be published. This implies that proposed rule of basing the consolidated group composition on the 2019 taxable year to calculate the amount of 2019 ATI that can be used in the 2020 taxable year will, relative to the alternative approach of using the composition in the 2020 taxable year, reduce the incentive for taxpayers to engage in costly mergers, acquisitions, or divestures to achieve a favorable tax result.

Number of Affected Taxpayers. The Treasury Department and the IRS estimate that approximately 34,000 corporate taxpayers filed a consolidated group tax return for tax year 2017. This represents an upper-bound of the number of taxpayers affected by the proposed rule as not all consolidated groups would need to calculate the amount of section 163(j) interest limitation in tax years 2019 and 2020.

D. Paperwork Reduction Act

The collection of information in these Proposed Regulations has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). 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. The collection of information in these Proposed Regulations has been submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)).

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

1. Collections of Information

The collections of information subject to the Paperwork Reduction Act in these

Proposed Regulations are in proposed §§ 1.163(j)–6(d)(5), 1.163(j)–6(g)(4), and 1.163(j)–7.

The collections of information in proposed §§ 1.163(j)–6(d)(5) and 1.163(j)–6(g)(4) are required to make two elections relating to changes made to section 163(j) by the CARES Act. The election under proposed § 1.163(j)–6(d)(5) is for a passthrough taxpayer to use the taxpayer's ATI for the last taxable year beginning in 2019 as its ATI for any taxable year beginning in 2020, in accordance with section 163(j)(10)(B). The election under proposed § 1.163(j)–6(g)(4) relates to excess business interest expense of a partnership for any taxable year beginning in 2019 that is allocated to a partner. Section 163(j)(10)(A)(ii)(II) provides that, unless the partner elects out, in 2020, the partner treats 50 percent of the excess business interest expense as not subject to the section 163(j) limitation. If the partner elects out, the partner treats all excess business interest expense as subject to the same limitations as other excess business interest expense allocated to the partner.

Revenue Procedure 2020–22 describes the time and manner for making these elections. For both elections, taxpayers make the election by timely filing a Federal income tax return or Form 1065, including extensions, an amended Federal income tax return, amended Form 1065, or administrative adjustment request, as applicable. More specifically, taxpayers complete the Form 8990, ''Limitation on Business Interest Expense under Section 163(j),'' using the taxpayer's 2019 ATI and/or not applying the rule in section 163(j)(10)(ii)(II), as applicable. No formal statements are required to make these elections. Accordingly, the reporting burden associated with the collections of information in proposed § 1.163(j)–6(d)(5) and –6(g)(4) will be reflected in the IRS Form 8990 Paperwork Reduction Act Submissions (OMB control number 1545–0123).

The collections of information in proposed § 1.163(j)–7 are required for taxpayers to make an election to apply section 163(j) to a CFC group (CFC group election) or an annual election to exempt a CFC or CFC group from the section 163(j) limitation (safe-harbor election). The elections are made by attaching a statement to the US shareholder's annual return. The CFC group election remains in place until revoked and may not be revoked for any period beginning prior to 60 months following the period for which it is made. The safe-harbor election is made on an annual basis.

Under § 1.964–1(c)(3)(i), no election of a foreign corporation is effectuated unless the controlling domestic shareholder provides a statement with their return and notice of the election to the minority shareholders under § 1.964–1(c)(3)(ii) and (iii). See also, § 1.952–2(b)–(c). These collections are necessary to ensure that the election is properly effectuated, and that taxpayers properly report the amount of interest that is potentially subject to the limitation.

2. Future Modifications to Forms To Collect Information

At this time, no modifications to any forms, including the Form 8990, ''Limitation on Business Interest Expense IRC 163(j),'' are proposed with regard to the elections under section 163(j)(10), or the CFC group or safe-harbor elections. The Treasury Department and the IRS are considering revisions to the Instructions for Form 8990 to reflect changes made to section 163(j)(10) regarding the elections under proposed §§ 1.163(j)–6(d)(5) and 1.163(j)–6(g)(4). For purposes of the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)), the reporting burden of Form 8990 is associated with OMB control number 1545–0123. In the 2018 Proposed Regulations, Form 8990 was estimated to be required by fewer than 92,500 taxpayers.

If an additional information collection requirement is imposed through these regulations in the future, for purposes of the Paperwork Reduction Act, any reporting burden associated with these regulations will be reflected in the aggregated burden estimates and the OMB control numbers for general income tax forms or the Form 8990, ''Limitation on Business Interest Expense Under Section 163(j)''.

The forms are available on the IRS website at:

Form	OMB No.	IRS website link
Form 1040	1545–0074	*https://www.irs.gov/pub/irs-pdf/f1040.pdf* (Instructions: *https://www.irs.gov/pub/irs-pdf/i1040gi.pdf).*
Form 1120	1545–0123	*https://www.irs.gov/pub/irs-pdf/f1120.pdf* (Instructions: *https://www.irs.gov/pub/irs-pdf/i1120.pdf).*
Form 1120S		*https://www.irs.gov/pub/irs-pdf/f1120s.pdf* (Instructions: *https://www.irs.gov/pub/irs-pdf/i1120s.pdf).*
Form 1065		*https://www.irs.gov/pub/irs-pdf/f1065.pdf* (Instructions: *https://www.irs.gov/pub/irs-pdf/i1065.pdf).*
Form 1120–REIT		*https://www.irs.gov/pub/irs-prior/f1120rei--2018.pdf* (Instructions: *https://www.irs.gov/pub/irs-pdf/i1120rei.pdf).*
Form 8990		*https://www.irs.gov/pub/irs-access/f8990_accessible.pdf* (Instructions: *https://www.irs.gov/pub/irs-pdf/i8990.pdf).*

In addition, when available, drafts of IRS forms are posted for comment at *https://apps.irs.gov/app/picklist/list/draftTaxForms.htm.* IRS forms are available at *https://www.irs.gov/forms-instructions.* Forms will not be finalized until after they have been approved by OMB under the PRA.

3. Burden Estimates

The following estimates for the collections of information in these proposed regulations are based on the most recently available Statistics of Income (SOI) tax data.

For the collection of income in proposed § 1.163(j)–6(d)(5), where a passthrough taxpayer elects to use the taxpayer's ATI for the last taxable beginning in 2019 as the taxpayer's ATI for any taxable year beginning in 2020, the most recently available 2017 SOI tax data indicates that, on the high end, the estimated number of respondents is 49,202. This number was determined by examining, for the 2017 tax year, Form 1065 and Form 1120–S filers with greater than $26 million in gross receipts that have reported interest expense, and do not have an NAICS code that is associated with a trade or business that normally would be excepted from the section 163(j) limitation.

For the collection of information under § 1.163(j)–6(g)(4), in which a partner elects out of treating 50 percent of any excess business interest expense allocated to the partner in 2019 as not subject to a limitation in 2020, the Treasury Department and the IRS estimate that only taxpayers that actively want to reduce their deductions will make this election. The application of the base erosion minimum tax under section 59A depends, in part, on the amount of a taxpayer's deductions.

Accordingly, the Treasury Department and the IRS estimate that taxpayers that are subject to both the base erosion minimum tax under section 59A and section 163(j) are the potential filers of this election. Using the 2017 SOI tax data, the Treasury Department estimate that 1,182 firms will make the election. This estimate was determined by examining three criteria: First, the number of taxpayers subject to section 59A, namely, C corporations with at least $500,000,000 in gross receipts, second, the portion of those taxpayers that do not have an NAICS code associated with a trade or business that is generally not subject to the section 163(j) limitation (2211 (electric power generation, transmission and distribution), 2212 (natural gas distribution), 2213 (water, sewage and other systems), 111 or 112 (farming), 531 (real property)), and, third, the portion of taxpayers satisfying the first two criteria that received a Form K–1, ''Partner's Share of Income, Deductions, Credits, etc.''

For the collections of information in proposed § 1.163(j)–7, namely the CFC and safe-harbor elections, and the corresponding notice under § 1.964–1(c)(3)(iii), the most recently available 2017 SOI tax data indicates that, on the high end, the estimated number of respondents is 4,980 firms. This number was determined by examining, for the 2017 tax year, Form 1040, Form 1120, Form 1120–S, and Form 1065 filers with greater than $26 million in gross receipts that filed a Form 5471, Information Return of U.S. Persons With Respect to Certain Foreign Corporations, where an interest expense amount was reported on Schedule C of the Form 5471.

The estimated number of respondents that could be subject to the collection of information for the CFC group or safe-harbor election is 4,980. The estimated annual burden per respondent/recordkeeper varies from 0 to 30 minutes, depending on individual circumstances, with an estimated average of 15 minutes. The estimated total annual reporting and/or recordkeeping burden is 1,245 hours (4,980 respondents × 15 minutes). The estimated annual cost burden to respondents is $95 per hour. Accordingly, we expect the total annual cost burden for the CFC group election and safe-harbor election statements to be $118,275 (4,980 * .25 * $95).

The Treasury Department and the IRS request comment on the assumptions, methodology, and burden estimates related to this information collection. Comments on the collection of information should be sent to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, SE:W:CAR:MP:T:T:SP, Washington, DC 20224. Comments on the collection of information should be received by November 2, 2020, which is 60 days after the date of filing for public inspection with the Office of the Federal Register.

Comments are specifically requested concerning—

Whether the proposed collection of information is necessary for the proper performance of the functions of the IRS, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collection of information;

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collection of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

II. Regulatory Flexibility Act

It is hereby certified that these Proposed Regulations, if adopted as final, will not have a significant economic impact on a substantial number of small entities.

This certification can be made because the Treasury Department and the IRS have determined that the number of small entities that are affected as a result of the regulations is not substantial. These rules do not disincentivize taxpayers from their operations, and any burden imposed is not significant because the cost of implementing the rules, if any, is low.

As discussed in the 2018 Proposed Regulations, section 163(j) provides exceptions for which many small entities will qualify. First, under section 163(j)(3), the limitation does not apply to any taxpayer, other than a tax shelter under section 448(a)(3), which meets the gross receipts test under section 448(c) for any taxable year. A taxpayer meets the gross receipts test under section 448(c) if the taxpayer has average annual gross receipts for the 3-taxable year period ending with the taxable year that precedes the current taxable year that do not exceed $26,000,000. The gross receipts threshold is indexed annually for inflation. Because of this threshold, the Treasury Department and the IRS project that entities with 3-year average gross receipts below $26 million will not be affected by these regulations except in rare cases.

Section 163(j) provides that certain trades or businesses are not subject to the limitation, including the trade or business of performing services as an employee, electing real property trades or businesses, electing farming businesses, and certain utilities as defined in section 163(j)(7)(A)(iv). Under the 2018 Proposed Regulations, taxpayers that otherwise qualified as real property trades or businesses or farming businesses that satisfied the small business exemption in section 448(c) were not eligible to make an election to be an electing real property trade or business or electing farming business. Under the Final Regulations, however, those taxpayers are eligible to make an election to be an electing real property trade or business or electing farming business. Additionally, the Final Regulations provide that certain utilities not otherwise excepted from the limitation can elect for a portion of their non-excepted utility trade or business to be excepted from the limitation. Any economic impact on any small entities as a result of the requirements in these Proposed Regulations, not just the requirements that impose a Paperwork Reduction Act burden, is not expected to be significant because the cost of implementing the rules, if any, is low.

The Treasury Department and the IRS do not have readily available data on the number of filers that are tax shelters, as defined in section 448(a)(3), that are potentially affected by these provisions. As described in more detail earlier in this Preamble, these Proposed Regulations cover several topics, including, but not limited to, debt financed distributions from passthrough entities, self-charged interest, the treatment of section 163(j) in relation to trader funds, the impact of section 163(j) on publicly traded partnerships, and the application of section 163(j) to United States shareholders of controlled foreign corporations and to foreign persons with effectively connected income in the United States.

The Treasury Department and the IRS do not have readily available data to determine the number of taxpayers affected by rules regarding self-charged interest because no reporting modules currently connect these payments by and from partnerships.

The Treasury Department and the IRS likewise do not have precise data on the number of taxpayers affected by rules regarding debt financed distributions. The Treasury Department and the IRS estimate that the number of taxpayers affected by the rules regarding debt-financed distributions is 50,036. This number was reached first by adding the number of Form 1065 filers that reported code W on line 13b of schedule K of the Form 1065, or approximately 410,996 using 2018 taxable year data, and the number of Form 1120–S filers that reported code S on line 12d of schedule K of the Form 1120–S, or approximately 89,367 using 2018 taxable year data. Those codes are used to report interest expense allocated to debt financed distributions. Using the result of the two numbers, 500,363 (410,996 + 89,367), produces overly broad results because the codes referenced above are used to report more than just interest expense allocated to debt financed distributions. Code W on line 13b of schedule K of the Form 1065 also is used to report at least nine other items, including, but not limited to, itemized deductions that Form 1040 or 1040–SR filers report on Schedule A, soil and water conservation expenditures, and the domestic productions activities deductions. Code S on line 12d of schedule K of the Form 1120–S also is used to report at least eleven other items, including, but not limited to, itemized deductions that Form 1040 or 1040–SR filers report on Schedule A, expenditures for the removal of architectural and transportation barriers for the elderly and disabled that the corporation elected to treat as a current expense, and film, television, and live theatrical production expenses. Considering the number of other items reported under those codes, the Treasury Department and the IRS estimate that approximately 10% of the filers using those codes report interest expense allocated to debt financed distributions (500,363 * 0.10 = 50,036).

Despite not having precise data, these rules do not impose a significant paperwork or implementation cost burden on taxpayers. Under Notice 89–35, taxpayers have been required to maintain books and records to properly report the tax treatment of interest associated with debt financed acquisitions and contributions by partners, and debt financed distributions to partners. Additional reporting requirements are needed to allow passthrough entities and their owners to comply with the interest tracing rules under § 1.163–8T. Without additional reporting, the mechanism for determining the tax treatment of interest under § 1.163–8T is burdensome and unclear. For example, in some cases, partners would need to report back to the partnership how they used debt financed distribution to allow the partnership to properly report its interest expense. This notice of proposed rules would provide consistent reporting and compliance by passthrough entities and their owners, which would reduce their overall burden. The estimated time to determine whether a distribution is a debt financed distribution and to comply with these rules would be 0 minutes to 30 minutes per taxpayer, depending on individual circumstances, for an average of 15 minutes. The 2018 monetization rates for this group of filers is $57.53. According, the Treasury Department and the IRS estimate the burden to be $719,642.77 (50,036 respondents * 0.25 hours * $57.53).

The Treasury Department and the IRS have determined that, on the high end, the rules regarding trading partnerships might affect approximately 309 small entities. This number was reached by determining, using data for the 2017 taxable year, the number of Form 1065 and Form 1065–B filers, with more than $26 million in gross receipts, that (1) completed Schedule B to Form 1065 and marked box b, c, or d in question 1 to denote limited partnership, limited liability company or limited liability partnership status; (2) have a North American Industry Classification System (NAICS) code starting with 5231, 5232, 5239 or 5259, and (3) do not have gross receipts exceeding the small business thresholds for the various NAICS codes. The following table provides a breakdown of the potentially affected taxpayers by NAICS code.

NAICS code	Titles	Gross receipts threshold	Number of respondents
5231	Securities and Commodity Contracts Intermediation and Brokerage, including Investment Bank and Securities Dealing; Securities Brokerage; Commodity Contract Dealing; Commodity Contracts Brokerage.	$41.5M	42
5232	Securities and Commodities Exchanges	41.5M	0
5239	Other Financial Investment Activities, including Miscellaneous Intermediation; Portfolio Management; Investment Advice; Trust, Fiduciary, and Custody Activities; Miscellaneous Financial Investment Activities.	41.5M	267
5259	Other Investment Pools and Funds, including Open-End Investment Funds; Trusts, Estates, and Agency Accounts; Other Financial Vehicles.	35M	[d]
Total Respondents.			309

Source: SOI Partnership Study, 2017.
[d] Data is suppressed based on disclosure rules detailed in Publication 1075.

Additionally, the Treasury Department and the IRS have determined that the rules regarding publicly traded partnerships might affect approximately 83 taxpayers. This number was reached by determining, using data for the 2017 taxable year, the number of Form 1065 and 1065–B filers with gross receipts exceeding $25 million that answered ''yes'' to question 5 on Schedule B to Form 1065 denoting that the entity is a publicly traded partnership.

As noted earlier, these Proposed Regulations do not impose any new collection of information on these entities. These Proposed Regulations actually assist small entities in meeting their filing obligations by providing definitive advice on which they can rely.

For the section 163(j)(10) elections for passthrough taxpayers under proposed §§ 1.163(j)–6(d)(5) and 1.163(j)–6(g)(4), most small taxpayers do not need to make the elections because, as discussed earlier, they are not subject to the section 163(j) limitation. For small taxpayers that are subject to the limitation, the cost to implement the election is low. Pursuant to Revenue Procedure 2020–22, these passthrough taxpayers simply complete the Form 8990 as if the election has been made. Accordingly, the burden of complying with the elections, if needed, is no different than for taxpayers who do not make the elections.

The persons potentially subject to proposed § 1.163(j)–7 are U.S. shareholders in one or more CFCs for which BIE is reported, and that (1) have average annual gross receipts for the 3-taxable year period ending with the taxable year that precedes the current taxable year exceeding $26,000,000, and (2) want to make the CFC group election or safe-harbor election. Proposed § 1.163(j)–7 requires such taxpayers to attach a statement to their return providing basic information regarding the CFC group or standalone CFC.

As discussed in the Paperwork Reduction Act section of this Preamble, the reporting burden for both statements is estimated at 0 to 30 minutes, depending on individual circumstances, with an estimated average of 15 minutes for all affected entities, regardless of size. The estimated monetized burden for compliance is $95 per hour.

For these reasons, the Treasury Department and the IRS have determined that these Proposed Regulations will not have a significant economic impact on a substantial number of small entities. Notwithstanding this certification, the Treasury Department and the IRS invite comments from interested members of the public on both the number of small entities affected and the economic impact on those small entities.

E. Unfunded Mandates Reform Act

Section 202 of the Unfunded Mandates Reform Act of 1995 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 was approximately $154 million. These Proposed Regulations do 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.

F. 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. These Proposed Regulations do not have federalism implications and do not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of the Executive Order.

Comments and Requests for a Public Hearing

Before these proposed amendments to the regulations are adopted as final regulations, consideration will be given to comments that are submitted timely to the IRS as prescribed in the preamble under the **ADDRESSES** section. The Treasury Department and the IRS request comments on all aspects of the proposed regulations. Any electronic comments submitted, and to the extent practicable any paper comments submitted, will be made available at *www.regulations.gov* or upon request.

A public hearing will be scheduled if requested in writing by any person who timely submits electronic or written comments. Requests for a public hearing are also encouraged to be made electronically. If a public hearing is scheduled, notice of the date and time for the public hearing will be published in the **Federal Register**. Announcement 2020–4, 2020–17 I.R.B. 667 (April 20, 2020), provides that until further notice, public hearings conducted by the IRS will be held telephonically. Any telephonic hearing will be made accessible to people with disabilities.

Drafting Information

The principal authors of these regulations are Susie Bird, Charles Gorham, Jaime Park, Joanna Trebat and Sophia Wang (Income Tax & Accounting), Anthony McQuillen, Adrienne M. Mikolashek, and William Kostak (Passthroughs and Special Industries), Azeka J. Abramoff (International), Russell Jones, and John Lovelace (Corporate), and Pamela Lew, Steven Harrison, and Michael Chin (Financial Institutions & Products). Other personnel from the Treasury Department and the IRS participated in their development.

Effect on Other Documents

Notice 89–35, 1989–1 C.B. 675, is proposed to be obsoleted.

Statement of Availability of IRS Documents

IRS Revenue Procedures, Revenue Rulings notices, and other guidance cited in this document 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.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 1 is proposed to be amended as follows:

PART 1—INCOME TAXES

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

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

■ **Par. 2.** Section 1.163–14 is added to read as follows:

§ 1.163–14 Allocation of interest expense among expenditures—Passthrough Entities.

(a) *In general*—(1) *Application.* This section prescribes rules for allocating interest expense associated with debt proceeds of a partnership or S corporation (a *passthrough entity*). In general, interest expense on a debt of a passthrough entity is allocated in the same manner as the debt to which such interest expense relates is allocated. Debt is allocated by tracing disbursements of the debt proceeds to specific expenditures. This section prescribes rules for tracing debt proceeds to specific expenditures of a passthrough entity.

(2) *Cross-references.* This paragraph provides the general manner in which interest expense of a passthrough entity is allocated. See paragraph (b) of this section for the treatment of interest expense allocated under the rules of this section, paragraph (c) for the manner in which debt proceeds of a passthrough entity are allocated and the manner in which interest expense allocated under this section is treated, paragraph (d) for rules relating to debt allocated under the rules of § 1.163–8T to distributions to owners of a passthrough entity, paragraph (e) for rules relating to debt repayments, paragraph (f) for rules relating to debt allocated under the rules of § 1.163–8T to expenditures for interests in passthrough entities, paragraph (g) for change of ownership rules for interest expense allocation

purposes, and paragraph (h) for examples.

(b) *Treatment of interest expense*—(1) *General rule.* Except as otherwise provided in section § 1.163(j)-8T(m), interest expense allocated under the rules of this section is treated in the following manner:

(i) Interest expense allocated to trade or business expenditures (as defined in paragraph (b)(2)(v) of this section) is taken into account under section 163(j) by the passthrough entity;

(ii) Interest expense allocated to other trade or business expenditures (as defined in paragraph (b)(2)(ii) of this section) is taken into account under the rules of § 1.163–8T, as applicable, by the passthrough entity owner allocated such interest expense;

(iii) Interest expense allocated to rental expenditures (as defined in paragraph (b)(2)(iv) of this section) is taken into account under the rules of § 1.163–8T, as applicable, by the passthrough entity owner allocated such interest expense;

(iv) Interest expense allocated to investment expenditures (as defined in paragraph (b)(2)(i) of this section) is taken into account under the rules of § 1.163–8T, as applicable, by the passthrough entity owner allocated such interest expense;

(v) Interest expense allocated to personal expenditures (as defined in paragraph (b)(2)(iii) of this section) is taken into account under the rules of § 1.163–8T, as applicable, by the passthrough entity owner allocated such interest expense;

(vi) Interest expense allocated to distributions to owners of a passthrough entity is taken into account in the manner provided under paragraph (d) of this section.

(2) *Definitions.* For purposes of this section—

(i) *Investment expenditure* means an expenditure defined in § 1.163–8T(b)(3), including any expenditure made with respect to a trade or business described in section 163(d)(5)(A)(ii) to the extent such expenditure is properly allocable under section 704(b) to partners that do not materially participate (within the meaning and for purposes of section 469) in the trade or business.

(ii) *Other trade or business expenditure* means an expenditure made with respect to any activity described in § 1.469–4(b)(1)(ii) and (iii).

(iii) *Personal expenditure* means an expenditure (other than a distribution) not described in paragraphs (b)(2)(i), (ii), (iv) and (v) of this section.

(iv) *Rental expenditure* means an expenditure made with respect to any activity described in § 1.469–4(b)(2) that is not a trade or business, as defined in § 1.163(j)–1(b)(44).

(v) *Trade or business expenditure* means an expenditure made with respect to a trade or business, as defined in § 1.163(j)–1(b)(44), except for an expenditure made with respect to a trade or business described in section 163(d)(5)(A)(ii) to the extent such expenditure is properly allocable under section 704(b) to partners that do not materially participate (within the meaning and for purposes of section 469) in the trade or business.

(c) *Allocation of debt and interest expense.* Except as otherwise provided in this section, the rules of § 1.163–8T apply to partnerships, S Corporations, and their owners.

(d) *Debt allocated to distributions by passthrough entities*—(1) *Allocation of distributed debt proceeds*—(i) *Available expenditures.* To the extent a passthrough entity has available expenditures (as defined in paragraph (d)(5)(ii) of this section), the passthrough entity shall first allocate distributed debt proceeds (as defined in paragraph (d)(5)(iii) of this section) to such available expenditures. If a passthrough entity has multiple available expenditures, the passthrough entity shall allocate distributed debt proceeds to such available expenditures in proportion to the amount of each expenditure.

(ii) *Debt financed distributions.* If a passthrough entity's distributed debt proceeds exceeds its available expenditures, the passthrough entity shall allocate such excess amount of distributed debt proceeds to distributions to owners of the passthrough entity (debt financed distributions).

(2) *Allocation of interest expense*—(i) *Interest expense allocated to debt financed distributions.* If distributed debt proceeds are allocated to distributions to owners of the passthrough entity (pursuant to paragraph (d)(1)(ii) of this section), the passthrough entity shall determine the portion of each passthrough entity owner's allocable interest expense that is debt financed distribution interest expense. The amount of a passthrough entity owner's *debt financed distribution interest expense* equals the lesser of such passthrough entity owner's allocable interest expense (as defined in paragraph (d)(5)(i) of this section) or the product of—

(A) The portion of the debt proceeds distributed to that particular passthrough entity owner; multiplied by

(B) A fraction, the numerator of which is the portion of the passthrough entity's distributed debt proceeds allocated to debt financed distributions (determined under paragraph (d)(1)(ii) of this section), and the denominator of which is the passthrough entity's total amount of distributed debt proceeds; multiplied by

(C) The distributed debt proceeds interest rate (as defined in paragraph (d)(5)(iv of this section).

(ii) *Interest expense allocated to available expenditures.* If distributed debt proceeds are allocated to available expenditures (pursuant to paragraph (d)(1)(i) of this section), the passthrough entity shall determine the portion of each passthrough entity owner's allocable interest expense that is expenditure interest expense. The amount of a passthrough entity owner's *expenditure interest expense* equals the product of—

(A) The portion of the passthrough entity's distributed debt proceeds allocated to available expenditures (determined under paragraph (d)(1)(i) of this section); multiplied by

(B) The distributed debt proceeds interest rate; multiplied by

(C) A fraction, the numerator of which is the excess of that particular passthrough entity owner's allocable interest expense over its debt financed distribution interest expense (determined under paragraph (d)(2)(i) of this section) (remaining interest expense), and the denominator of which is aggregate of all the passthrough owners' remaining interest expense amounts.

(iii) *Excess interest expense.* To the extent a passthrough entity owner's allocable interest expense is not treated as either debt financed distribution interest expense (determined under paragraph (d)(2)(i) of this section) or expenditure interest expense (determined under paragraph (d)(2)(ii) of this section), such allocable interest expense is *excess interest expense.*

(3) *Tax treatment of interest expense*—(i) *Debt financed distribution interest expense.* The tax treatment of a passthrough entity owner's debt financed distribution interest expense (determined under paragraph (d)(2)(i) of this section), if any, shall be determined by the passthrough entity owner under the rules of § 1.163–8T, as applicable, in accordance with such passthrough entity owner's use of its portion of the passthrough entity's distributed debt proceeds. The passthrough entity shall separately state the amount of each owner's debt financed distribution interest expense. Debt financed distribution interest expense is not treated as interest expense of the entity for purposes of this section.

(ii) *Expenditure interest expense.* The tax treatment of a passthrough entity owner's expenditure interest expense (determined under paragraph (d)(2)(ii) of this section), if any, shall be determined based on how the distributed debt proceeds were allocated among available expenditures (pursuant to paragraph (d)(1)(i) of this section). For example, if distributed debt proceeds are allocated to a rental activity under paragraph (d)(1)(i) of this section, the interest expense associated with such debt should be taken into account by the passthrough entity in computing income or loss from the rental activity that is reported to the owner.

(iii) *Excess interest expense.* The tax treatment of a passthrough entity owner's excess interest expense (determined under paragraph (d)(2)(iii) of this section), if any, shall be determined by allocating the distributed debt proceeds among all the assets of the passthrough entity, pro-rata, based on the adjusted basis of such assets. For purposes of the preceding sentence, the passthrough entity shall use either the adjusted tax bases of its assets reduced by any debt of the passthrough entity allocated to such assets, or determine its adjusted basis in its assets in accordance with the rules in § 1.163(j)–10(c)(5)(i), reduced by any debt of the passthrough entity allocated to such assets. Once a passthrough entity chooses a method for determining its adjusted basis in its assets for this purpose, the passthrough entity must consistently apply the same method in all subsequent tax years. Any assets purchased in the same taxable year as the distribution (such that the expenditure for those assets was taken into account in § 1.163–14(b)(1)) are not included in this allocation.

(4) *Treatment of transfers of interests in a passthrough entity by an owner that received a debt financed distribution*—(i) *In general.* In the case of a transfer of an interest in a passthrough entity, any debt financed distribution interest expense of the transferor shall be treated as excess interest expense by the transferee. However, in the case of a transfer of an interest in a passthrough entity to a person who is related to the transferor, any debt financed distribution interest expense of the transferor shall continue to be treated as debt financed distribution interest expense by the related party transferee, and the tax treatment of such debt financed distribution expense under paragraph (d)(3) of this section shall be the same to the related party transferee as it was to the transferor. The term related party means any person who bears a relationship to the taxpayer which is described in section 267(b) or 707(b)(1).

(ii) *Anti-avoidance rule.* Arrangements entered into with a principal purpose of avoiding the rules of this paragraph, including the transfer of an interest in a passthrough entity by an owner who treated a portion of its allocable interest expense as debt financed distribution interest expense to an unrelated party pursuant to a plan to transfer the interest back to the owner who received the debt financed distribution interest expense or to a party who is related to the owner who received the debt financed distribution interest expense, may be disregarded or recharacterized by the Commissioner of the IRS to the extent necessary to carry out the purposes of this paragraph.

(5) *Definitions.* For purposes of this paragraph—

(i) *Allocable interest expense* means a passthrough entity owner's share of interest expense associated with the distributed debt proceeds allocated under section 704 or section 1366(a).

(ii) *Available expenditure* means an expenditure of a passthrough entity described in paragraph (b)(2) of this section made in the same taxable year of the entity as the distribution, to the extent that debt proceeds (including other distributed debt proceeds) are not otherwise allocated to such expenditure.

(iii) *Distributed debt proceeds* means debt proceeds of a passthrough entity that are allocated under § 1.163–8T and this section to distributions to owners of the passthrough entity in a taxable year. If debt proceeds from multiple borrowings are allocated under § 1.163–8T to distributions to owners of the passthrough entity in a taxable year, then all such borrowings are treated as a single borrowing for purposes of this section.

(iv) *Distributed debt proceeds interest rate* means a fraction, the numerator of which is the amount of interest expense associated with distributed debt proceeds, and the denominator of which is the amount of distributed debt proceeds.

(e) *Repayment of passthrough entity debt*—(1) *In general.* If any portion of passthrough entity debt is repaid at a time when such debt is allocated to more than one expenditure, the debt is treated for purposes of this section as repaid in the following order:

(i) Amounts allocated to one or more expenditures described in paragraph (b)(2)(iii);

(ii) Amounts allocated to one or more expenditures described in paragraph (b)(2)(i) (relating to investment expenditures as defined in § 1.163–8T(b)(3));

(iii) Amounts allocated to one or more expenditures described in paragraphs (b)(2)(ii) and (iv) (relating to expenditures with respect to any activities described in § 1.469–4(b)(1)(ii) and (iii), and § 1.469–4(b)(2)); and

(iv) Amounts allocated to one or more expenditures described in paragraph (b)(2)(v) (generally relating to expenditures made with respect to a trade or business as defined in § 1.163(j)–1(b)(44)).

(2) *Repayment of debt used to finance a distribution.* Any repayment of debt of a passthrough entity that has been allocated to debt financed distributions under paragraph (d)(1)(ii) of this section and to one or more available expenditures under paragraph (d)(1)(i) of this section may, at the option of the passthrough entity, be treated first as a repayment of the portion of the debt that had been allocated to such debt financed distributions.

(f) *Debt allocated to expenditures for interests in passthrough entities.* In the case of debt proceeds allocated under the rules of § 1.163–8T and this section to contributions to the capital of or to the purchase of an interest in a passthrough entity, the character of the debt proceeds and any associated interest expense shall be determined by allocating the debt proceeds among the adjusted tax bases of the entity's assets. For purposes of this paragraph, the owner must allocate the debt proceeds either in proportion to the relative adjusted tax basis of the entity's assets reduced by any debt allocated to such assets, or based on the adjusted basis of the entity's assets in accordance with the rules in § 1.163(j)–10(c)(5)(i) reduced by any debt allocated to such assets. Once the owner chooses a method for allocating the debt proceeds for this purpose, the owner must consistently apply the same method in all subsequent tax years. Individuals shall report interest expense paid or incurred in connection with debt-financed acquisitions on their individual income tax return in accordance with the asset to which the interest expense is allocated under this paragraph.

(g) *Change in ownership.* Any transfer of an ownership interest in a passthrough entity is not a reallocation event for purposes of § 1.163–8T(j), except as provided for in paragraph (d)(4) of this section.

(h) *Examples*—(1) *Example 1*—(i) *Facts.* A (an individual) and B (an individual) are partners in partnership PRS. PRS conducts two businesses; a manufacturing business, which is a trade or business as defined in § 1.163(j)–1(b)(44) (manufacturing), and a separate commercial real estate leasing business, which is an activity described in § 1.469–4(b)(2) (leasing). In Year 1, PRS borrowed $100,000 from an unrelated third-party lender (the loan). Other than the loan, PRS does not have any outstanding debt. During Year 1, PRS paid $80,000 in manufacturing expenses, $120,000 in leasing expenses, and made a $100,000 distribution to A, the proceeds of which A used to make a personal expenditure. Under § 1.163–8T, PRS treated the $100,000 of loan proceeds as having been distributed to A. As a result, in Year 1 PRS had $200,000 of available expenditures (as defined in paragraph (d)(5)(ii) of this section) and $100,000 of distributed debt proceeds (as defined in paragraph (d)(5)(iii) of this section). PRS paid $10,000 in interest expense that accrued during Year 1 on the loan, and allocated such interest expense under section 704(b) equally to A and B ($5,000 each). Thus, A and B each had $5,000 of allocable interest expense (as defined in paragraph (d)(5)(i) of this section).

(ii) *Applicability.* Because PRS treated all $100,000 of the loan proceeds as having been distributed under § 1.163–8T, PRS allocated all $10,000 of the interest expense associated with the loan to the distribution. Thus, pursuant to paragraph (b)(1)(vi) of this section, PRS must determine the tax treatment of such $10,000 of interest expense in the manner provided in paragraph (d) of this section.

(iii) *Debt allocated to distributions.* Under paragraph (d)(1)(i) of this section, to the extent PRS has available expenditures (as defined under paragraph (d)(5)(ii) of this section), it must allocate any distributed debt proceeds (as defined under paragraph (d)(5)(iii) of this section) to such available expenditures. Here, PRS has distributed debt proceeds of $100,000 and available expenditures of $200,000 (manufacturing expenditures of $80,000, plus leasing expenditures of $120,000). Thus, PRS allocates all $100,000 of the distributed debt proceeds to available expenditures as follows: $40,000 to manufacturing expenditures ($100,000 × ($80,000/$200,000)) and $60,000 to leasing expenditures ($100,000 × ($120,000/$200,000)). Because the amount of PRS's distributed debt proceeds is less than its available expenditures, none of the distributed debt proceeds are allocated to debt financed distributions pursuant to paragraph (d)(1)(ii) of this section.

(iv) *Allocation of interest expense.* Because all of PRS's distributed debt proceeds are allocated to available expenditures (pursuant to paragraph (d)(1)(i) of this section), A and B each treat all $5,000 of their allocable interest expense as expenditure interest expense.

(v) *Tax treatment of interest expense.* Pursuant to paragraph (d)(3)(ii) of this section, each partner treats its expenditure interest expense (determined under paragraph (d)(2)(ii) of this section) in the same manner as the distributed debt proceeds that were allocated to available expenditures under paragraph (d)(1)(i) of this section. Thus, A's $5,000 of expenditure interest expense comprises of $2,000 of business interest expense ($5,000 × ($40,000/$100,000)) and $3,000 of interest expense allocated to rental expenditures ($5,000 × ($60,000/$100,000)). B's $5,000 of expenditure interest expense similarly comprises of $2,000 of business interest expense and $3,000 of interest expense allocated to rental expenditures. As a result, $4,000 of interest expense associated with the distributed debt proceeds (A's $2,000 plus B's $2,000 of expenditure interest expense treated as business interest expense) is business interest expense of PRS, subject to section 163(j) at the PRS level.

TABLE 1 TO PARAGRAPH (h)(2)(vii)

	Partner A	Partner B
Allocable interest expense:		
Debt financed distribution interest expense:		
N/A	$0	$0
Expenditure interest expense:		
Business interest (to PRS)	2,000	2,000
Rental activity interest expense	3,000	3,000
Excess interest expense:		
N/A	0	0
Total	5,000	5,000

(2) *Example 2*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (h)(1)(i) of this section, except PRS did not have any rental expenditures in Year 1. As a result, in Year 1 PRS had $80,000 of available expenditures (as defined in paragraph (d)(5)(ii) of this section) and $100,000 of distributed debt proceeds (as defined in paragraph (d)(5)(iii) of this section).

(ii) *Applicability.* Because PRS treated all $100,000 of the loan proceeds as having been distributed to A under § 1.163–8T, PRS allocated all $10,000 of the interest expense associated with the loan to the distribution. Thus, pursuant to paragraph (b)(1)(vi) of this section, PRS must determine the tax treatment of such $10,000 of interest expense in the manner provided in paragraph (d) of this section.

(iii) *Debt allocated to distributions.* Under paragraph (d)(1)(i) of this section, to the extent PRS has available expenditures (as defined under paragraph (d)(5)(ii) of this section), it must allocate any distributed debt proceeds (as defined under paragraph (d)(5)(i) of this section) to such available expenditures. Here, PRS has distributed debt proceeds of $100,000 and available expenditures of $80,000. Thus, $80,000 of the distributed debt proceeds are allocated to such available expenditures. Pursuant to paragraph (d)(1)(ii) of this section, PRS allocates the remaining $20,000 of the distributed debt proceeds to debt financed distributions.

(iv) *Allocation of interest expense—debt financed distribution interest expense.* Pursuant to paragraph (d)(2)(i) of this section, A treats $2,000 of its allocable interest expense as debt financed distribution interest expense, which is the lesser of $5,000 or $2,000 ((A) the portion of debt proceeds distributed to A ($100,000), multiplied by (B) a fraction, the numerator of which is the portion of PRS's distributed debt proceeds allocated to debt financed distributions pursuant to paragraph (d)(1)(ii) of this section ($20,000), and the denominator of which is PRS's total amount of distributed debt proceeds ($100,000), multiplied by (C) the distributed debt proceeds interest rate, as defined in paragraph (d)(5)(iii) of this section, of 10% (the amount of interest expense associated with distributed debt proceeds ($10,000), divided by the amount of distributed debt proceeds ($100,000))) and B treats $0 of its allocable interest expense as debt financed distribution interest expense, which is the lesser of $5,000 or $0 ((A) $0 × (B) 20% × (C) 10%).

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Table 2 to paragraph (h)(2)(iv)

The portion of partner A's allocable interest expense that is debt financed distribution interest expense equals the lesser of:					
Partner A's allocable interest expense; or				=	$5,000
(d)(2)(i)(A)	Portion of debt proceeds allocated to partner A	=	$100,000		
(d)(2)(i)(B)	$\frac{\text{Debt financed distributions}}{\text{Distributed debt proceeds}}$	=	$\frac{\$20{,}000}{\$100{,}000}$		
(d)(2)(i)(C)	$\frac{\text{Distributed debt proceeds}}{\text{interest rate}}$	=	$\frac{\$10{,}000}{\$100{,}000}$		
The product of (d)(2)(i)(A), (B), and (C).				=	$2,000

Table 3 to paragraph (h)(2)(iv)

The portion of partner B's allocable interest expense that is debt financed distribution interest expense equals the lesser of:					
Partner B's allocable interest expense; or				=	$5,000
(d)(2)(i)(A)	Portion of debt proceeds allocated to partner B	=	$0		
(d)(2)(i)(B)	$\frac{\text{Debt financed distributions}}{\text{Distributed debt proceeds}}$	=	$\frac{\$20{,}000}{\$100{,}000}$		
(d)(2)(i)(C)	$\frac{\text{Distributed debt proceeds}}{\text{interest rate}}$	=	$\frac{\$10{,}000}{\$100{,}000}$		
The product of (d)(2)(i)(A), (B), and (C).				=	$0

(v) *Allocation of interest expense—expenditure interest expense.* Pursuant to paragraph (d)(2)(ii) of this section, A treats $3,000 of its allocable interest expense as expenditure interest expense ((A) the portion of PRS's distributed debt proceeds allocated to available expenditures pursuant to paragraph (d)(1)(i) of this section ($80,000), multiplied by (B) the distributed debt proceeds interest rate (10%), multiplied by (C) a fraction, the numerator of which is A's remaining interest expense (that is, the excess of A's allocable interest expense ($5,000) over its debt financed distribution interest expense as determined under paragraph (d)(2)(i) of this section ($2,000)), and the denominator of which is the aggregate of A's and B's remaining interest expense amounts ($3,000 + $5,000)) and B treats $5,000 of its allocable interest expense as expenditure interest expense ((A) $80 × (B) 10% × (C) 62.5%).

Table 4 to paragraph (h)(2)(v)			
The portion of partner A's allocable interest expense that is expenditure interest expense equals the product of:			
(d)(2)(ii)(A)	Distributed debt proceeds allocated to available expenditures	=	$80,000
(d)(2)(ii)(B)	Distributed debt proceeds interest rate	=	$10,000 / $100,000
(d)(2)(ii)(C)	Partner A's remaining interest expense / Aggregate remaining interest expense	=	$3,000 / $8,000
The product of (d)(2)(ii)(A), (B), and (C).		=	$3,000

Table 5 to paragraph (h)(2)(v)			
The portion of partner B's allocable interest expense that is expenditure interest expense equals the product of:			
(d)(2)(ii)(A)	Distributed debt proceeds allocated to available expenditures	=	$80,000
(d)(2)(ii)(B)	Distributed debt proceeds interest rate	=	$10,000 / $100,000
(d)(2)(ii)(C)	Partner B's remaining interest expense / Aggregate remaining interest expense	=	$5,000 / $8,000
The product of (d)(2)(ii)(A), (B), and (C).		=	$5,000

(vi) *Allocation of interest expense—excess interest expense.* Neither partner treats any of its allocable interest expense as excess interest expense under paragraph (d)(2)(iii) of this section.

(vii) *Tax treatment of interest expense.* Pursuant to paragraph (d)(3)(i) of this section, each partner determines the tax treatment of its debt financed distribution interest expense (determined under paragraph (d)(2)(i) of this section) based on its use of the distributed debt proceeds. Because A used its $100,000 of distributed debt proceeds on a personal expenditure, A's $2,000 of debt financed distribution interest expense is personal interest subject to section 163(h) at A's level. Pursuant to paragraph (d)(3)(ii) of this section, each partner treats its expenditure interest expense (determined under paragraph (d)(2)(ii) of this section) in the same manner as the distributed debt proceeds that were allocated to available expenditures under paragraph (d)(1)(i) of this section. Thus, all $3,000 of A's expenditure interest expense and all $5,000 of B's expenditure interest expense is business interest expense. As a result, $8,000 interest expense associated with the distributed debt proceeds (A's $3,000 plus B's $5,000 of expenditure interest expense treated as business interest expense) is business interest expense of PRS, subject to section 163(j) at the PRS level.

TABLE 6 TO PARAGRAPH (h)(2)(vii)

	Partner A	Partner B
Allocable interest expense;		
Debt financed distribution interest expense:		
Personal interest	$2,000	$0
Expenditure interest expense:		
Business interest (to PRS)	3,000	5,000
Excess interest expense:		
N/A	0	0
Total	5,000	5,000

(3) *Example 3*—(i) *Facts.* The facts are the same as in *Example 2* in paragraph (h)(2)(i) of this section, except PRS paid $20,000 in manufacturing expenses, made a distribution of $75,000 to A (the proceeds of which A used on a personal expenditure), and made a distribution of $25,000 to B (the proceeds of which B used on a trade or business expenditure). As a result, in Year 1 PRS had $20,000 of available expenditures (as defined in paragraph (d)(5)(ii) of this section) and $100,000 of distributed debt proceeds (as defined in paragraph (d)(5)(iii) of this section). The $20,000 manufacturing expenditure was to acquire assets used in PRS's manufacturing business. At the end of Year 1, the adjusted tax basis of PRS's assets used in manufacturing was $720,000 and the adjusted tax basis of PRS's assets used in leasing was $200,000. In addition, at the end of Year 1, the adjusted basis of PRS's assets held for investment (within the meaning of section 163(d)(5)) was $100,000.

(ii) *Applicability.* Because PRS treated all $100,000 of the loan proceeds as having been distributed under § 1.163–8T, PRS allocated all $10,000 of the interest expense associated with the loan to the distribution. Thus, pursuant to paragraph (b)(1)(vi) of this section, PRS must determine the tax treatment of such $10,000 of interest expense in the manner provided in paragraph (d) of this section.

(iii) *Debt allocated to distributions.* Under paragraph (d)(1)(i) of this section, to the extent PRS has available expenditures (as defined under paragraph (d)(5)(ii) of this section), it must allocate any distributed debt proceeds (as defined under paragraph (d)(5)(i) of this section) to such available expenditures. Here, PRS has distributed debt proceeds of $100,000 and available expenditures of $20,000. Thus, PRS allocates $20,000 of the distributed debt proceeds to available expenditures. Pursuant to paragraph (d)(1)(ii) of this section, PRS allocates the remaining $80,000 of distributed debt proceeds to debt financed distributions.

(iv) *Allocation of interest expense—debt financed distribution interest expense.* Pursuant to paragraph (d)(2)(i) of this section, A treats $5,000 of its allocable interest expense as debt financed distribution interest expense, which is the lesser of $5,000 or $6,000 ((A) $75,000 × (B) 80% × (C) 10%) and B treats $2,000 of its allocable interest expense as debt financed distribution interest expense, which is the lesser of $5,000 or $2,000 ((A) $25,000 × (B) 80% × (C) 10%).

Table 7 to paragraph (h)(3)(iv)

The portion of partner A's allocable interest expense that is debt financed distribution interest expense equals the lesser of:

Partner A's allocable interest expense; or				=	$5,000
(d)(2)(i)(A)	Portion of debt proceeds allocated to partner A	=	$75,000		
(d)(2)(i)(B)	$\frac{\text{Debt financed distributions}}{\text{Distributed debt proceeds}}$	=	$\frac{\$80,000}{\$100,000}$		
(d)(2)(i)(C)	Distributed debt proceeds interest rate	=	$\frac{\$10,000}{\$100,000}$		
The product of (d)(2)(i)(A), (B), and (C).				=	$6,000

Table 8 to paragraph (h)(3)(iv)

The portion of partner B's allocable interest expense that is debt financed distribution interest expense equals the lesser of:

Partner B's allocable interest expense; or				=	$5,000
(d)(2)(i)(A)	Portion of debt proceeds allocated to partner B	=	$25,000		
(d)(2)(i)(B)	$\frac{\text{Debt financed distributions}}{\text{Distributed debt proceeds}}$	=	$\frac{\$80,000}{\$100,000}$		
(d)(2)(i)(C)	Distributed debt proceeds interest rate	=	$\frac{\$10,000}{\$100,000}$		
The product of (d)(2)(i)(A), (B), and (C).				=	$2,000

(v) *Allocation of interest expense—expenditure interest expense.* Pursuant to paragraph (d)(2)(ii) of this section, A does not treat any of its allocable interest expense as expenditure interest expense ((A) $20,000 × (B) 10% × (C) 0%) and B treats $2,000 of its allocable interest expense as expenditure interest expense ((A) $20,000 × (B) 10% × (C) 100%).

Table 9 to paragraph (h)(3)(v)			
The portion of partner A's allocable interest expense that is expenditure interest expense equals the product of:			
(d)(2)(ii)(A)	Distributed debt proceeds allocated to available expenditures	=	$20,000
(d)(2)(ii)(B)	Distributed debt proceeds interest rate	=	$10,000 / $100,000
(d)(2)(ii)(C)	Partner A's remaining interest expense / Aggregate remaining interest expense	=	$0 / $3,000
The product of (d)(2)(ii)(A), (B), and (C).		=	$0

Table 10 to paragraph (h)(3)(v)			
The portion of partner B's allocable interest expense that is expenditure interest expense equals the product of:			
(d)(2)(ii)(A)	Distributed debt proceeds allocated to available expenditures	=	$20,000
(d)(2)(ii)(B)	Distributed debt proceeds interest rate	=	$10,000 / $100,000
(d)(2)(ii)(C)	Partner B's remaining interest expense / Aggregate remaining interest expense	=	$3,000 / $3,000
The product of (d)(2)(ii)(A), (B), and (C).		=	$2,000

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(vi) *Allocation of interest expense—excess interest expense.* Pursuant to paragraph (d)(2)(iii) of this section, A does not treat any of its allocable interest expense as excess interest expense ($5,000 of allocable interest expense, less $5,000 of debt financed distribution interest expense, less $0 of expenditure interest expense) and B treats $1,000 of its allocable interest expense as excess interest expense ($5,000 of allocable interest expense, less $2,000 of debt financed distribution interest expense, less $2,000 of expenditure interest expense).

(vii) *Tax treatment of interest expense.* Pursuant to paragraph (d)(3)(i) of this section, each partner determines the tax treatment of its debt financed distribution interest expense based on its use of the distributed debt proceeds. A used its share of the distributed debt proceeds to make personal expenditures. Thus, A's $5,000 of debt financed distribution interest expense is subject to section 163(h) at A's level. B used its share of the distributed debt proceeds to make trade or business expenditures. Thus, B's $2,000 of debt financed distribution interest expense is subject to section 163(j) at B's level. Pursuant to paragraph (d)(3)(ii) of this section, B treats its $2,000 of expenditure interest expense in the same manner as the distributed debt proceeds were allocated to available expenditures under paragraph (d)(1)(i) of this section. Thus, B's $2,000 of expenditure interest expense is business interest expense, subject to section 163(j) at the level of PRS. Pursuant to paragraph (d)(3)(iii) of this section, B determines the tax treatment of its $1,000 of excess interest expense by allocating distributed debt proceeds among the adjusted basis of PRS's assets, reduced by any debt allocated to such assets. For purposes of paragraph (d)(3)(iii) of this section, PRS's has $700,000 ($720,000 − $20,000 debt proceeds allocated to such assets) of basis in its manufacturing assets, $200,000 of basis in its leasing assets, and $100,000 of basis in its assets held for investment. Thus, B's $1,000 of excess interest expense is treated as $700 of business interest expense subject to 163(j) at the PRS level, $200 of interest expense related to a rental activity, and $100 of investment interest expense.

TABLE 11 TO PARAGRAPH (h)(3)(vii)

	Partner A	Partner B
Allocable interest expense:		
Debt financed distribution interest expense:		
Personal interest:	$5,000	$0
Business interest (but not to PRS)	0	2,000

TABLE 11 TO PARAGRAPH (h)(3)(vii)—Continued

	Partner A	Partner B
Expenditure interest expense:		
Business interest (to PRS)	0	2,000
Excess interest expense:		
Business interest (to PRS):	0	700
Rental activity interest expense	0	200
Investment interest expense	0	100
Total	5,000	5,000

(4) *Example 4.* The facts are the same as in *Example 2* in paragraph (h)(2)(i) of this section. In Year 2, A sells its interest in PRS to C. C is not related to either A or B under the rules of either section 267(b) or section 707(b)(1). No facts have changed with respect to PRS's loan. Under these facts, and only for purposes of this section, C's share of the debt financed distribution interest expense will be treated as excess interest expense pursuant to paragraph (d)(4)(i) of this section. Accordingly, C will determine the character of its share of this interest expense by allocating the debt proceeds associated with this interest expense among the assets of PRS under paragraph (d)(3)(iii) of this section.

(5) *Example 5.* The facts are the same as in *Example 4* in paragraph (h)(4) of this section, except that C is a party that is related to A under the rules of either section 267(b) or section 707(b)(1). Under these facts, and only for purposes of this section, A's $2,000 of debt financed distribution interest expense shall, pursuant to paragraph (d)(4)(i) of this section, continue to be treated as debt financed distribution interest expense of C, subject to the same tax treatment as it was to the transferor (personal interest expense).

(6) *Example 6.* The facts are the same as in *Example 2* in paragraph (h)(2)(i) of this section, except that in Year 2 B sells its interest in PRS to D. D is not related to either A or B under the rules of either section 267(b) or section 707(b)(1). No other facts have changed with respect to PRS's loan. Under these facts, the tax treatment of the expenditure interest expense does not change with respect to PRS or any of the partners as a result of the ownership change pursuant to paragraph (g) of this section. Accordingly, the tax treatment of the expenditure interest expense allocable to D under section 704(b) is identical to the expenditure interest expense that had been allocable to B prior to the sale.

(7) *Example 7*—(i) *Facts.* A (an individual) and B (an individual) are equal shareholders in S corporation X. X conducts a manufacturing business, which is a trade or business as defined in § 1.163(j)–1(b)(44) (manufacturing). In Year 1, X borrowed $100,000 from an unrelated third-party lender (the loan). Other than the loan, X does not have any outstanding debt. During Year 1, X paid $100,000 in manufacturing expenses and made a $50,000 distribution to each of its shareholders, A and B, which each shareholder used to make a personal expenditure. Under § 1.163–8T, X treated all $100,000 of the loan proceeds as having been distributed to A and B. As a result, in Year 1 X had $100,000 of available expenditures (as defined in paragraph (d)(5)(ii) of this section) and $100,000 of distributed debt proceeds (as defined in paragraph (d)(5)(iii) of this section). X paid $10,000 in interest expense that accrued during Year 1 on the loan, and allocated such interest expense under section 1366(a) equally to A and B ($5,000 each). Thus, A and B each had $5,000 of allocable interest expense (as defined in paragraph (d)(5)(i) of this section).

(ii) *Applicability.* Because X treated all $100,000 of the loan proceeds as having been distributed to A and B under § 1.163–8T, PRS allocated all $10,000 of the interest expense associated with the loan to the distributions. Thus, pursuant to paragraph (b)(1)(vi) of this section, PRS must determine the tax treatment of such $10,000 of interest expense in the manner provided in paragraph (d) of this section.

(iii) *Debt allocated to distributions.* Under paragraph (d)(1)(i) of this section, to the extent X has available expenditures (as defined under paragraph (d)(5)(ii) of this section), it must allocate any distributed debt proceeds (as defined under paragraph (d)(5)(iii) of this section) to such available expenditures. Here, X has distributed debt proceeds of $100,000 and available expenditures of $100,000. Thus, PRS allocates all $100,000 of the distributed debt proceeds to available expenditures

(iv) *Allocation of interest expense.* Because all of X's distributed debt proceeds are allocated to available expenditures (pursuant to paragraph (d)(1)(i) of this section), A and B each treat all $5,000 of their allocable interest expense as expenditure interest expense.

(v) *Tax treatment of interest expense.* Pursuant to paragraph (d)(3)(ii) of this section, each partner treats its expenditure interest expense (determined under paragraph (d)(2)(ii) of this section) in the same manner as the distributed debt proceeds that were allocated to available expenditures under paragraph (d)(1)(i) of this section. Thus, A's $5,000 of expenditure interest expense and B's $5,000 of expenditure interest expense is treated as business interest expense of X, subject to section 163(j) at X's level.

TABLE 12 TO PARAGRAPH (h)(7)(v)

	Partner A	Partner B
Allocable interest expense:		
Debt financed distribution interest expense:		
N/A	$0	$0
Expenditure interest expense:		
Business interest (to X)	5,000	5,000
Excess interest expense:		
N/A	0	0
Total	5,000	5,000

(h) *Applicability date.* This section applies to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], provided that they consistently apply the rules of this section to that taxable year and each subsequent taxable year.

■ **Par. 3.** Section 1.163–15 is added to read as follows:

§ 1.163–15 Debt Proceeds Distributed from Any Taxpayer Account or from Cash.

(a) *In general.* Regardless of paragraphs (c)(4) and (5) of § 1.163–8T, in the case of debt proceeds deposited in an account, a taxpayer that is applying § 1.163–8T or § 1.163–14 may treat any expenditure made from any account of the taxpayer, or from cash, within 30 days before or 30 days after debt proceeds are deposited in any account of the taxpayer as made from such proceeds to the extent thereof. Similarly, in the case of debt proceeds received in cash, a taxpayer that is applying § 1.163–8T or § 1.163–14 may treat any expenditure made from any account of the taxpayer, or from cash, within 30 days before or 30 days after debt proceeds are received in cash as made from such proceeds to the extent thereof. For purposes of this section, terms used have the same meaning as in § 1.163–8T(c)(4) and (5).

(b) *Applicability date.* This section applies to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], provided that they consistently apply the rules of this section to that taxable year and each subsequent taxable year.

■ **Par. 4.** As added in a final rule published elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.163(j)–0 is amended by:

■ 1. Revising the entries for § 1.163(j)–1(b)(1)(iv)(B), (b)(22)(iii)(F), and (b)(35);

■ 2. Adding entries for §§ 1.163(j)–1(b)(1)(iv)(E), (c)(4), and (c)(4)(i) and (ii);

■ 3. Adding an entry for § 1.163(j)–2(d)(3);

■ 4. Revising the entries for §§ 1.163(j)–2(k) and 1.163(j)–6(c)(1) and (2);

■ 5. Adding an entry for § 1.163(j)–6(d)(3), (4), and (5) and (e)(5);

■ 6. Revising the entries for §§ 1.163(j)–6(f)(1)(iii), (g)(4), (h)(4) and (5), (j), and (n) and 1.163(j)–7;

■ 7. Adding an entry for § 1.163(j)–8;

■ 8. Revising the entries for § 1.163(j)–10(c)(5)(ii)(D) and (f).

The revisions and additions read as follows:

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■ **Par. 5.** As added in a final rule published elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.163(j)–1 is amended by:

■ 1. Revising paragraph (b)(1)(iv)(B).
■ 2. Adding paragraphs (b)(1)(iv)(E), (b)(22)(iii)(F), and (b)(35)
■ 3. In paragraph (c)(1), removing ''paragraphs (c)(2) and (3)'' from the first sentence and adding ''paragraphs (c)(2), (3), and (4)'' in its place.
■ 4. Adding paragraph (c)(4).

The revisions and additions read as follows:

§ 1.163(j)–1 Definitions.

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(b) * * *
(1) * * *
(iv) * * *

(B) *Deductions by members of a consolidated group*—(*1*) *In general.* If paragraph (b)(1)(ii)(C), (D), or (E) of this section applies to adjust the tentative taxable income of a taxpayer, and if the taxpayer does not use the computation method in paragraph (b)(1)(iv)(E) of this section, the amount of the adjustment under paragraph (b)(1)(ii)(C) of this section equals the greater of the allowed or allowable depreciation, amortization, or depletion of the property, as provided under section 1016(a)(2), for any member of the consolidated group for the taxable years beginning after December 31, 2017, and before January 1, 2022, with respect to such property.

(*2*) *Application of the alternative computation method.* If paragraph (b)(1)(ii)(C), (D), or (E) of this section applies to adjust the tentative taxable income of a taxpayer, and if the taxpayer uses the computation method in paragraph (b)(1)(iv)(E) of this section, the amount of the adjustment under paragraph (b)(1)(ii)(C) of this section equals the lesser of:

(i) Any gain recognized on the sale or other disposition of such property by the taxpayer (or, if the taxpayer is a member of a consolidated group, the consolidated group); and

(ii) The greater of the allowed or allowable depreciation, amortization, or depletion of the property, as provided under section 1016(a)(2), for the taxpayer (or, if the taxpayer is a member of a consolidated group, the consolidated group) for the taxable years beginning after December 31, 2017, and before January 1, 2022, with respect to such property.

* * * * *

(E) *Alternative computation method.* If paragraph (b)(1)(ii)(C), (D), or (E) of this section applies to adjust the tentative taxable income of a taxpayer, the taxpayer may compute the amount of the adjustments required by such paragraph using the formulas in paragraph (b)(1)(iv)(E)(*1*), (*2*), and (*3*) of this section, respectively, provided that the taxpayer applies such formulas to all dispositions for which an adjustment is required under paragraph (b)(1)(ii)(C), (D), or (E) of this section.

(*1*) *Alternative computation method for property dispositions.* With respect to the sale or other disposition of property, the lesser of:

(*i*) Any gain recognized on the sale or other disposition of such property by the taxpayer (or, if the taxpayer is a member of a consolidated group, the consolidated group); and

(*ii*) The greater of the allowed or allowable depreciation, amortization, or depletion of the property, as provided under section 1016(a)(2), for the taxpayer (or, if the taxpayer is a member of a consolidated group, the consolidated group) for the taxable years beginning after December 31, 2017, and before January 1, 2022, with respect to such property.

(*2*) *Alternative computation method for dispositions of member stock.* With respect to the sale or other disposition of stock of a member of a consolidated group by another member, the lesser of:

(*i*) Any gain recognized on the sale or other disposition of such stock; and

(*ii*) The investment adjustments under § 1.1502–32 with respect to such stock that are attributable to deductions described in paragraph (b)(1)(ii)(C) of this section.

(*3*) *Alternative computation method for dispositions of partnership interests.* With respect to the sale or other disposition of an interest in a partnership, the lesser of (*i*) any gain recognized on the sale or other disposition of such interest, and (*ii*) the taxpayer's (or, if the taxpayer is a consolidated group, the consolidated group's) distributive share of deductions described in paragraph (b)(1)(ii)(C) of this section with respect to property held by the partnership at the time of such sale or other disposition to the extent such deductions were allowable under section 704(d).

* * * * *

(22) * * *

(iii) * * *

(F) *Section 163(j) interest dividends*—(*1*) *In general.* Except as otherwise provided in this paragraph (b)(22)(iii)(F), a section 163(j) interest dividend is treated as interest income.

(*2*) *Limitation on amount treated as interest income.* A shareholder may not treat any part of a section 163(j) interest dividend as interest income to the extent the amount of the section 163(j) interest dividend exceeds the excess of the amount of the entire dividend that includes the section 163(j) interest dividend over the sum of the conduit amounts other than interest-related dividends under section 871(k)(1)(C) and section 163(j) interest dividends that affect the shareholder's treatment of that dividend.

(*3*) *Conduit amounts.* For purposes of paragraph (b)(22)(iii)(F)(*2*) of this section, the term *conduit amounts* means, with respect to any category of income (including tax-exempt interest) earned by a RIC for a taxable year, the amounts identified by the RIC (generally in a designation or written report) in connection with dividends paid by the RIC for that taxable year that are subject to a limit determined by reference to that category of income. For example, a RIC's conduit amount with respect to its net capital gain is the amount of capital gain dividends that the RIC pays under section 852(b)(3)(C).

(*4*) *Holding period.* Except as provided in paragraph (b)(22)(iii)(F)(*5*) of this section, no dividend is treated as interest income under paragraph (b)(22)(iii)(F)(*1*) of this section if the dividend is received with respect to a share of RIC stock—

(*i*) That is held by the shareholder for 180 days or less (taking into account the principles of section 246(c)(3) and (4)) during the 361-day period beginning on the date which is 180 days before the date on which the share becomes ex-dividend with respect to such dividend; or

(*ii*) To the extent that the shareholder is under an obligation (whether pursuant to a short sale or otherwise) to make related payments with respect to positions in substantially similar or related property.

(*5*) *Exception to holding period requirement for money market funds and certain regularly declared dividends.* Paragraph (b)(22)(iii)(F)(*4*)(*i*) of this section does not apply to dividends distributed by any RIC regulated as a money market fund under 17 CFR 270.2a–7 (Rule 2a–7 under the 1940 Act) or to regular dividends paid by a RIC that declares section 163(j) interest dividends on a daily basis in an amount equal to at least 90 percent of its excess section 163(j) interest income, as defined in paragraph (b)(35)(iv)(E) of this section, and distributes such dividends on a monthly or more frequent basis.

* * * * *

(35) *Section 163(j) interest dividend.* The term *section 163(j) interest dividend* means a dividend paid by a RIC for a taxable year for which section 852(b) applies to the RIC, to the extent described in paragraph (b)(35)(i) or (ii) of this section, as applicable.

(i) *In general.* Except as provided in paragraph (b)(35)(ii) of this section, a section 163(j) interest dividend is any dividend, or part of a dividend, that is reported by the RIC as a section 163(j) interest dividend in written statements furnished to its shareholders.

(ii) *Reduction in the case of excess reported amounts.* If the aggregate reported amount with respect to the RIC for the taxable year exceeds the excess section 163(j) interest income of the RIC for such taxable year, the section 163(j) interest dividend is—

(A) The reported section 163(j) interest dividend amount; reduced by

(B) The excess reported amount that is allocable to that reported section 163(j) interest dividend amount.

(iii) *Allocation of excess reported amount*—(A) *In general.* Except as provided in paragraph (b)(35)(iii)(B) of this section, the excess reported amount, if any, that is allocable to the reported section 163(j) interest dividend amount is that portion of the excess reported amount that bears the same ratio to the excess reported amount as the reported section 163(j) interest dividend amount bears to the aggregate reported amount.

(B) *Special rule for noncalendar year RICs.* In the case of any taxable year that does not begin and end in the same calendar year, if the post-December reported amount equals or exceeds the excess reported amount for that taxable year, paragraph (b)(35)(iii)(A) of this section is applied by substituting ''post-December reported amount'' for ''aggregate reported amount,'' and no excess reported amount is allocated to any dividend paid on or before December 31 of such taxable year.

(iv) *Definitions.* The following definitions apply for purposes of this paragraph (b)(35):

(A) *Reported section 163(j) interest dividend amount.* The term *reported section 163(j) interest dividend amount* means the amount of a dividend distribution reported to the RIC's shareholders under paragraph (b)(35)(i) of this section as a section 163(j) interest dividend.

(B) *Excess reported amount.* The term *excess reported amount* means the excess of the aggregate reported amount over the RIC's excess section 163(j) interest income for the taxable year.

(C) *Aggregate reported amount.* The term *aggregate reported amount* means the aggregate amount of dividends reported by the RIC under paragraph (b)(35)(i) of this section as section 163(j) interest dividends for the taxable year (including section 163(j) interest dividends paid after the close of the taxable year described in section 855).

(D) *Post-December reported amount.* The term *post-December reported* *amount* means the aggregate reported amount determined by taking into account only dividends paid after December 31 of the taxable year.

(E) *Excess section 163(j) interest income.* The term *excess section 163(j) interest income* means, with respect to a taxable year of a RIC, the excess of the RIC's business interest income for the taxable year over the sum of the RIC's business interest expense for the taxable year and the RIC's other deductions for the taxable year that are properly allocable to the RIC's business interest income.

(v) *Example*—(A) *Facts.* X is a domestic C corporation that has elected to be a RIC. For its taxable year ending December 31, 2021, X has $100x of business interest income (all of which is qualified interest income for purposes of section 871(k)(1)(E)) and $10x of dividend income (all of which is qualified dividend income within the meaning of section 1(h)(11) and would be eligible for the dividends received deduction under section 243, determined as described in section 854(b)(3)). X has $10x of business interest expense and $20x of other deductions. X has no other items for the taxable year. On December 31, 2021, X pays a dividend of $80x to its shareholders, and reports, in written statements to its shareholders, $71.82x as a section 163(j) interest dividend; $10x as dividends that may be treated as qualified dividend income or as dividends eligible for the dividends received deduction; and $72.73x as interest-related dividends under section 871(k)(1)(C). Shareholder A, a domestic C corporation, meets the holding period requirements in paragraph (b)(22)(iii)(F)(*4*) of this section with respect to the stock of X, and receives a dividend of $8x from X on December 31, 2021.

(B) *Analysis.* X determines that $18.18x of other deductions are properly allocable to X's business interest income. X's excess section 163(j) interest income under paragraph (b)(35)(iv)(E) of this section is $71.82x ($100x business interest income − ($10x business interest expense + $18.18x other deductions allocated) = $71.82x). Thus, X may report up to $71.82x of its dividends paid on December 31, 2021, as section 163(j) interest dividends to its shareholders. X may also report up to $10x of its dividends paid on December 31, 2021, as dividends that may be treated as qualified dividend income or as dividends that are eligible for the dividends received deduction. X determines that $9.09x of interest expense and $18.18x of other deductions are properly allocable to X's qualified interest income. Therefore, X may report up to $72.73x of its dividends paid on December 31, 2021, as interest-related dividends under section 871(k)(1)(C) ($100x qualified interest income − $27.27x deductions allocated = $72.73x). A treats $1x of its $8x dividend as a dividend eligible for the dividends received deduction and no part of the dividend as an interest-related dividend under section 871(k)(1)(C). Therefore, under paragraph (b)(22)(iii)(F)(*2*) of this section, A may treat $7x of the section 163(j) interest dividend as interest income for purposes of section 163(j) ($8x dividend − $1x conduit amount = $7x limitation).

* * * * *

(c) * * *

(4) *Alternative computation for certain adjustments to tentative taxable income, and section 163(j) interest dividends*—(i) *Alternative computation for certain adjustments to tentative taxable income.* Paragraphs (b)(1)(iv)(B) and (E) of this section apply to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **Federal Register**]. Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules in paragraphs (b)(1)(iv)(B) and (E) of this section to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **Federal Register**], so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4, to that taxable year and each subsequent taxable year.

(ii) *Section 163(j) interest dividends.* Paragraphs (b)(22)(iii)(*F*) and (b)(35) of this section apply to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **Federal Register**]. Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules in paragraphs (b)(22)(iii)(F) and (b)(35) of this section for a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **Federal Register**], so long as the taxpayers and their related parties consistently apply the rules of the section 163(j) regulations.

■ **Par. 6.** As added in a final rule published elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.163(j)–2 is amended by:

■ 1. Adding paragraphs (b)(3)(iii) and (iv) and (d)(3).

■ 2. Redesignating paragraph (k) as paragraph (k)(1).

■ 3. Adding a new subject heading for paragraph (k).

■ 4. Revising the subject heading of redesignated paragraph (k)(1).

■ 5. Adding paragraph (k)(2).

The additions and revision read as follows:

§ 1.163(j)–2 Deduction for business interest expense limited.

* * * * *

(b) * * *

(3) * * *

(iii) *Transactions to which section 381 applies.* For purposes of the election described in paragraph (b)(3)(i) of this section, and subject to the limitation in paragraph (b)(3)(ii) of this section, the 2019 ATI of the acquiring corporation in a transaction to which section 381 applies equals the amount of the acquiring corporation's ATI for its last taxable year beginning in 2019.

(iv) *Consolidated groups.* For purposes of the election described in paragraph (b)(3)(i) of this section, and subject to the limitation in paragraph (b)(3)(ii) of this section, the 2019 ATI of a consolidated group equals the amount of the consolidated group's ATI for its last taxable year beginning in 2019.

* * * * *

(d) * * *

(3) *Determining a syndicate's loss amount.* For purposes of section 163(j), losses allocated under section 1256(e)(3)(B) and § 1.448–1T(b)(3) are determined without regard to section 163(j). See also § 1.1256(e)–2(b).

* * * * *

(k) *Applicability dates.*

(1) *In general.* * * *

(2) *Paragraphs (b)(3)(iii), (b)(3)(iv), and (d)(3).* Paragraphs (b)(3)(iii) and (iv) and (d)(3) of this section apply to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of paragraphs (b)(3)(iii) and (iv) of this section to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], provided that they consistently apply the rules of paragraphs (b)(3)(iii) and (iv) of this section and the rules in the section 163(j) regulations for that taxable year and for each subsequent taxable year. Taxpayers and their related parties, within the meaning of sections 267(b) and 707(b), may choose to apply the rules of paragraph (d)(3) of this section to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE

IN THE **FEDERAL REGISTER**], provided that they consistently apply the rules of paragraph (d)(3) of this section for that taxable year and for each subsequent taxable year.

■ **Par. 7.** As added in a final rule published elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.163(j)–6 is amended by:

■ 1. Adding paragraphs (c)(1) and (2), (d)(3) through (5), (e)(5) and (6), (f)(1)(iii), (g)(4), (h)(4) and (5), (j), (l)(4)(iv), (n), and (o)(24) through (29).

■ 2. Redesignating paragraph (p) as paragraph (p)(1).

■ 3. Adding a new subject heading for paragraph (p).

■ 4. Revising the subject heading of newly redesignated paragraph (p)(1).

■ 5. Adding paragraph (p)(2).

The additions and revision read as follows:

§ 1.163(j)–6 Application of the business interest deduction limitation to partnerships and subchapter S corporations.

* * * * *

(c) * * *

(1) *Modification of business interest income for partnerships.* The business interest income of a partnership generally is determined in accordance with § 1.163(j)–1(b)(3). To the extent that interest income of a partnership that is properly allocable to trades or businesses that are per se non-passive activities and is allocated to partners that do not materially participate (within the meaning of section 469), as described in section 163(d)(5)(A)(ii), such interest income shall not be considered business interest income for purposes of determining the section 163(j) limitation of a partnership pursuant to § 1.163(j)–2(b). A per se non-passive activity is an activity that is not treated as a passive activity for purposes of section 469 regardless of whether the owners of the activity materially participate in the activity.

(2) *Modification of business interest expense for partnerships.* The business interest expense of a partnership generally is determined in accordance with § 1.163(j)–1(b)(2). To the extent that interest expense of a partnership that is properly allocable to trades or businesses that are per se non-passive activities is allocated to partners that do not materially participate within the meaning of section 469, as described in section 163(d)(5)(A)(ii), such interest expense shall not be considered business interest expense for purposes of determining the section 163(j) limitation of a partnership pursuant to § 1.163(j)–2(b).

* * * * *

(d) * * *

(3) *Section 743(b) adjustments and publicly traded partnerships.* Solely for purposes of § 1.163(j)–6, a publicly traded partnership, as defined in § 1.7704–1, shall treat the amount of any section 743(b) adjustment of a purchaser of a partnership unit that relates to a remedial item that the purchaser inherits from the seller as an offset to the related section 704(c) remedial item. For this purpose, § 1.163(j)–6(e)(2)(ii) applies. See *Example 25* in paragraph (o)(25) of this section.

(4) *Modification of adjusted taxable income for partnerships.* The adjusted taxable income of a partnership generally is determined in accordance with § 1.163(j)–1(b)(1). To the extent that the items comprising the adjusted taxable income of a partnership are properly allocable to trades or businesses that are per se non-passive activities and are allocated to partners that do not materially participate (within the meaning of section 469), as described in section 163(d)(5)(A)(ii), such partnership items shall not be considered adjusted taxable income for purposes of determining the section 163(j) limitation of a partnership pursuant to § 1.163(j)–2(b).

(5) *Election to use 2019 adjusted taxable income for taxable years beginning in 2020.* In the case of any taxable year beginning in 2020, a partnership may elect to apply this section by substituting its adjusted taxable income for the last taxable year beginning in 2019 for the adjusted taxable income for such taxable year. See § 1.163(j)–2(b)(4) for the time and manner of making or revoking this election. An electing partnership determines each partner's allocable ATI (as defined in paragraph (f)(2)(ii) of this section) pursuant to paragraph (j)(9) of this section in the same manner as an upper-tier partnership. See *Example 34* in paragraph (o)(34) of this section.

* * * * *

(e) * * *

(5) *Partner basis items, remedial items, and publicly traded partnerships.* Solely for purposes of § 1.163(j)–6, a publicly traded partnership, as defined in § 1.7704–1, shall either allocate gain that would otherwise be allocated under section 704(c) based on a partner's section 704(b) sharing ratios, or, for purposes of allocating cost recovery deductions under section 704(c), determine a partner's remedial items, as defined in § 1.163(j)–6(b)(3), based on an allocation of the partnership's asset basis (inside basis) items among its partners in proportion to their share of corresponding section 704(b) items (rather than applying the traditional method, described in § 1.704–3(b)). See *Example 24* in paragraph (o)(24) of this section.

(6) *Partnership deductions capitalized by a partner.* The ATI of a partner is increased by the portion of such partner's allocable share of qualified expenditures (as defined in section 59(e)(2)) to which an election under section 59(e) applies.

* * * * *

(f) * * *

(1) * * *

(iii) *Exception applicable to publicly traded partnerships.* Publicly traded partnerships, as defined in § 1.7704–1, do not apply the rules in paragraph (f)(2) of this section to determine a partner's share of section 163(j) excess items. Rather, publicly traded partnerships determine a partner's share of section 163(j) excess items by applying the same percentage used to determine the partner's share of the corresponding section 704(b) items that comprise ATI.

* * * * *

(g) * * *

(4) *Special rule for taxable years beginning in 2019 and 2020.* In the case of any excess business interest expense of a partnership for any taxable year beginning in 2019 that is allocated to a partner under paragraph (f)(2) of this section, 50 percent of such excess business interest expense (§ 1.163(j)–6(g)(4) business interest expense) is treated as business interest expense that, notwithstanding paragraph (g)(2) of this section, is paid or accrued by the partner in the partner's first taxable year beginning in 2020. Additionally, § 1.163(j)–6(g)(4) business interest expense is not subject to the section 163(j) limitation at the level of the partner. For purposes of paragraph (h)(1) of this section, any § 1.163(j)–6(g)(4) business interest expense is, similar to deductible business interest expense, taken into account before any excess business interest expense. This paragraph applies after paragraph (n) of this section. If a partner disposes of a partnership interest in the partnership's 2019 or 2020 taxable year, § 1.163(j)–6(g)(4) business interest expense is deductible by the partner and thus does not result in a basis increase under paragraph (h)(3) of this section. See *Example 35* and *Example 36* in paragraphs (o)(35) and (o)(36), respectively, of this section. A taxpayer may elect to not have this provision apply. The rules and procedures regarding the time and manner of making, or revoking, such an election are provided in Revenue Procedure 2020–22, 2020–18 I.R.B. 745, and may

be further modified through other guidance (see §§ 601.601(d) and 601.602 of this chapter).

* * * * *

(h) * * *

(4) *Partner basis adjustments upon liquidating distribution.* For purposes of paragraph (h)(3) of this section, a disposition includes a distribution of money or other property by the partnership to a partner in complete liquidation of the partner's interest in the partnership. However, a current distribution of money or other property by the partnership to a continuing partner is not a disposition for purposes of paragraph (h)(3) of this section.

(5) *Partnership basis adjustments upon partner dispositions.* If a partner (transferor) disposes of its partnership interest, the partnership shall increase the adjusted basis of partnership property by an amount equal to the amount of the increase required under paragraph (h)(3) (or, if the transferor is a partnership, (j)(5)(ii)) of this section (if any) to the adjusted basis of the partnership interest being disposed of by the transferor. Such increase in the adjusted basis of partnership property (§ 1.163(j)–6(h)(5) basis adjustment) shall be allocated among capital gain property of the partnership in the same manner as a positive section 734(b) adjustment. However, the increase in the adjusted basis of any partnership property resulting from a § 1.163(j)–6(h)(5) basis adjustment is not depreciable or amortizable under any section of the Code, regardless of whether the partnership property allocated such § 1.163(j)–6(h)(5) basis adjustment is otherwise generally depreciable or amortizable. In general, a partnership allocates its § 1.163(j)–6(h)(5) basis adjustment immediately before the disposition (simultaneous with the transferor's basis increase required under paragraph (h)(3) or (j)(5)(ii) of this section). However, if the disposition was the result of a distribution by the partnership of money or other property to the transferor in complete liquidation of the transferor's interest in the partnership, the partnership allocates its § 1.163(j)–6(h)(5) basis adjustment among its properties only after it has allocated its section 734(b) adjustment (if any) among its properties. See *Example 31* in paragraph (o)(31) of this section.

* * * * *

(j) *Tiered partnerships*—(1) *Purpose.* The purpose of this section is to provide guidance regarding the treatment of business interest expense of a partnership (lower-tier partnership) that is allocated to a partner that is a partnership (upper-tier partnership). Specifically, this section clarifies that disparities are not created between an upper-tier partner's basis in its upper-tier partnership interest and such partner's share of the adjusted basis of upper-tier partnership's property following the allocation of excess business interest expense from lower-tier partnership to upper-tier partnership. Further, these rules disallow any deduction for business interest expense that was formerly excess business interest expense to any person that is not the specified partner of such business interest expense. See *Example 27* through *Example 30* in paragraphs (o)(27) through (30), respectively.

(2) *Section 704(b) capital account adjustments.* If lower-tier partnership pays or accrues business interest expense and allocates such business interest expense to upper-tier partnership, then both upper-tier partnership and any direct or indirect partners of upper-tier partnership shall, solely for purposes of section 704(b) and the regulations thereunder, treat such business interest expense as a section 705(a)(2)(B) expenditure. Any section 704(b) capital account reduction resulting from such treatment occurs regardless of whether such business interest expense is characterized under this section as excess business interest expense or deductible business interest expense by lower-tier partnership. If upper-tier partnership subsequently treats any excess business interest expense allocated from lower-tier partnership as business interest expense paid or accrued pursuant to paragraph (g) of this section, the section 704(b) capital accounts of any direct or indirect partners of upper-tier partnership are not further reduced.

(3) *Basis adjustments of upper-tier partnership.* If lower-tier partnership allocates excess business interest expense to upper-tier partnership, then upper-tier partnership reduces its basis in lower-tier partnership pursuant to paragraph (h)(2) of this section. Upper-tier partnership partners do not, however, reduce the bases of their upper-tier partnership interests pursuant to paragraph (h)(2) of this section until upper-tier partnership treats such excess business interest expense as business interest expense paid or accrued pursuant to paragraph (g) of this section.

(4) *Treatment of excess business interest expense allocated by lower-tier partnership to upper-tier partnership.* Except as provided in paragraph (j)(7) of this section, if lower-tier partnership allocates excess business interest expense to upper-tier partnership and such excess business interest expense is not suspended under section 704(d), then upper-tier partnership shall treat such excess business interest expense (UTP EBIE) as a nondepreciable capital asset, with a fair market value of zero and basis equal to the amount by which upper-tier partnership reduced its basis in lower-tier partnership pursuant to paragraph (h)(2) of this section due to the allocation of such excess business interest expense. The fair market value of UTP EBIE, described in the preceding sentence, is not adjusted by any revaluations occurring under § 1.704–1(b)(2)(iv)(f). In addition to generally treating UTP EBIE as having a basis component in excess of fair market value and, thus, built-in loss property, upper-tier partnership shall also treat UTP EBIE as having a carryforward component associated with it. The carryforward component of UTP EBIE shall equal the amount of excess business interest expense allocated from lower-tier partnership to upper-tier partnership under paragraph (f)(2) of this section that is treated as such under paragraph (h)(2) of this section by upper-tier partnership. If an allocation of excess business interest expense from lower-tier partnership is treated as UTP EBIE of upper-tier partnership, upper-tier partnership shall treat such allocation of excess business interest expense from lower-tier partnership as UTP EBIE until the occurrence of an event described in paragraph (j)(5) of this section.

(5) *UTP EBIE conversion events*—(i) *Allocation to upper-tier partnership by lower-tier partnership of excess taxable income (or excess business interest income).* To the extent upper-tier partnership is allocated excess taxable income (or excess business interest income) from lower-tier partnership, or paragraph (m)(3) of this section applies, upper-tier partnership shall—

(A) First, apply the rules in paragraph (g) of this section to its UTP EBIE, using any reasonable method (including, for example, FIFO and LIFO) to determine which UTP EBIE is treated as business interest expense paid or accrued pursuant paragraph (g) of this section. If paragraph (m)(3) of this section applies, upper-tier partnership shall treat all of its UTP EBIE from lower-tier partnership as business interest expense paid or accrued.

(B) Second, with respect to any UTP EBIE treated as business interest expense paid or accrued in paragraph (j)(5)(i)(A) of this section, allocate any business interest expense that was formerly such UTP EBIE to its specified partner. For purposes of this section, the term specified partner refers to the partner of upper-tier partnership that, due to the initial allocation of excess business interest expense from lower-tier partnership to upper-tier partnership, was required to reduce its section 704(b) capital account pursuant to paragraph (j)(2) of this section. Similar principles apply if the specified partner of such business interest expense is itself a partnership. See paragraph (j)(6) of this section for rules that apply if a specified partner disposes of its partnership interest.

(C) Third, in the manner provided in paragraph (j)(7)(ii) (or (iii), as the case may be) of this section, take into account any negative basis adjustments under section 734(b) previously made to the UTP EBIE treated as business interest expense paid or accrued in paragraph (j)(5)(i)(A) of this section. Additionally, persons treated as specified partners with respect to the UTP EBIE treated as business interest expense paid or accrued in paragraph (j)(5)(i)(A) shall take any negative basis adjustments under section 743(b) into account in the manner provided in paragraph (j)(7)(ii) (or (iii), as the case may be) of this section.

(ii) *Upper-tier partnership disposition of lower-tier partnership interest.* If upper-tier partnership disposes of a lower-tier partnership interest (transferred interest), upper-tier partnership shall—

(A) First, apply the rules in paragraph (h)(3) of this section (except as provided in paragraphs (j)(5)(ii)(B) and (C) of this section), using any reasonable method (including, for example, FIFO and LIFO) to determine which UTP EBIE is reduced pursuant paragraph (h)(3) of this section.

(B) Second, increase the adjusted basis of the transferred interest immediately before the disposition by the total amount of the UTP EBIE that was reduced in paragraph (j)(5)(ii)(A) of this section (the amount of UTP EBIE proportionate to the transferred interest).

(C) Third, in the manner provided in paragraph (j)(7)(iv) of this section, take into account any negative basis adjustments under sections 734(b) and 743(b) previously made to the UTP EBIE that was reduced in (A) earlier.

(6) *Disposition of a specified partner's partnership interest*—(i) *General rule.* If a specified partner (transferor) disposes of an upper-tier partnership interest (or an interest in a partnership that itself is a specified partner), the portion of any UTP EBIE to which the transferor's status as specified partner relates is not reduced pursuant to paragraph (j)(5)(ii) of this section. Rather, such UTP EBIE attributable to the interest disposed of is retained by upper-tier partnership and the transferee is treated as the specified partner for purposes of this section with respect to such UTP EBIE. Thus, upper-tier partnership must allocate any business interest expense that was formerly such UTP EBIE to the transferee. However, see paragraph (j)(8) of this section for rules regarding the deductibility of such transferee's business interest expense that was formerly UTP EBIE.

(ii) *Special rules*—(A) *Distribution in liquidation of a specified partner's partnership interest.* If a specified partner receives a distribution of property in complete liquidation of an upper-tier partnership interest, the portion of UTP EBIE of upper-tier partnership attributable to the liquidated interest shall not have a specified partner. If a specified partner (transferee) receives a distribution of an interest in upper-tier partnership in complete liquidation of a partnership interest, the transferee is the specified partner with respect to UTP EBIE of upper-tier partnership only to the same extent it was prior to the distribution. Similar principles apply where an interest in a partnership that is a specified partner is distributed in complete liquidation of a transferee's partnership interest. See paragraph (j)(8) of this section for rules regarding the treatment of UTP EBIE that does not have a specified partner.

(B) *Contribution of a specified partner's partnership interest.* If a specified partner (transferor) contributes an upper-tier partnership interest to a partnership (transferee), the transferee is treated as the specified partner with respect to the portion of the UTP EBIE attributable to the contributed interest. Following the transaction, the transferor continues to be the specified partner with respect to the UTP EBIE attributable to the contributed interest. Similar principles apply where an interest in a partnership that is a specified partner is contributed to a partnership.

(7) *Effect of basis adjustments allocated to UTP EBIE*—(i) *In general.* Negative basis adjustments under sections 734(b) and 743(b) allocated to UTP EBIE do not affect the carryforward component (described in paragraph (j)(4) of this section) of such UTP EBIE. Rather, negative basis adjustments under sections 734(b) and 743(b) affect only the basis component of such UTP EBIE. For purposes of §§ 1.743–1(d), 1.755–1(b), and 1.755–1(c), the amount of tax loss that would be allocated to a transferee from a hypothetical disposition by upper-tier partnership of its UTP EBIE equals the adjusted basis of the UTP EBIE to which the transferee's status as specified partner relates. Additionally, solely for purposes of § 1.755–1(b), upper-tier partnership shall treat UTP EBIE as an ordinary asset of upper-tier partnership.

(ii) *UTP EBIE treated as deductible business interest expense.* If UTP EBIE that was allocated a negative section 734(b) adjustment is subsequently treated as deductible business interest expense, then such deductible business interest expense does not result in a deduction to the upper-tier partnership or the specified partner of such deductible business interest expense. If UTP EBIE that was allocated a negative section 743(b) adjustment is subsequently treated as deductible business interest expense, the specified partner of such deductible business interest expense recovers any negative section 743(b) adjustment attributable to such deductible business interest expense (effectively eliminating any deduction for such deductible business interest expense).

(iii) *UTP EBIE treated as excess business interest expense.* If UTP EBIE that was allocated a negative section 734(b) or 743(b) adjustment is subsequently treated as excess business interest expense, the specified partner's basis decrease in its upper-tier partnership interest required under paragraph (h)(2) of this section is reduced by the amount of the negative section 734(b) or 743(b) adjustment previously made to such excess business interest expense. If such excess business interest expense is subsequently treated as business interest expense paid or accrued by the specified partner, no deduction shall be allowed for any of such business interest expense. If the specified partner of such excess business interest expense is a partnership, such excess business interest expense is considered UTP EBIE that was previously allocated a negative section 734(b) adjustment for purposes of this section.

(iv) *UTP EBIE reduced due to a disposition.* If UTP EBIE that was allocated a negative section 734(b) or 743(b) adjustment is reduced pursuant to paragraph (j)(5)(ii)(A) of this section, the amount of upper-tier partnership's basis increase under paragraph (j)(5)(ii)(B) of this section to the disposed of lower-tier partnership interest is reduced by the amount of the negative section 734(b) or 743(b) adjustment previously made to such UTP EBIE.

(8) *Anti-loss trafficking*—(i) *Transferee specified partner.* No deduction shall be allowed to any

transferee specified partner for any business interest expense derived from a transferor's share of UTP EBIE. For purposes of this section, the term transferee specified partner refers to any specified partner that did not reduce its section 704(b) capital account due to the initial allocation of excess business interest expense from lower-tier partnership to upper-tier partnership pursuant to paragraph (j)(2) of this section. However, the transferee described in paragraph (j)(6)(ii)(B) of this section is not a transferee specified partner for purposes of this section. If pursuant to paragraph (j)(5)(i)(B) of this section a transferee specified partner is allocated business interest expense derived from a transferor's share of UTP EBIE (business interest expense to which the partner's status as transferee specified partner relates), the transferee specified partner is deemed to recover a negative section 743(b) adjustment with respect to, and in the amount of, such business interest expense and takes such negative section 743(b) adjustment into account in the manner provided in paragraph (j)(7)(ii) (or (iii), as the case may be) of this section, regardless of whether a section 754 election was in effect or a substantial built-in loss existed at the time of the transfer by which the transferee specified partner acquired the transferred interest. However, to the extent a negative section 734(b) or 743(b) adjustment was previously made to such business interest expense, the transferee specified partner does not recover an additional negative section 743(b) adjustment pursuant to this paragraph.

(ii) *UTP EBIE without a specified partner.* If UTP EBIE does not have a specified partner (as the result of a transaction described in paragraph (j)(6)(ii)(A) of this section), upper-tier partnership shall not allocate any business interest expense that was formerly such UTP EBIE to its partners. Rather, for purposes of applying paragraph (f)(2) of this section, upper-tier partnership shall treat such business interest expense as the allocable business interest expense (as defined in paragraph (f)(2)(ii) of this section) of a § 1.163(j)–6(j)(8)(ii) account. Additionally, if UTP EBIE that does not have a specified partner (as the result of a transaction described in paragraph (j)(6)(ii)(A) of this section) is treated as paid or accrued pursuant to paragraph (g) of this section, upper-tier partnership shall make a § 1.163(j)–6(h)(5) basis adjustment to its property in the amount of the adjusted basis (if any) of such UTP EBIE at the time such UTP EBIE is treated as business interest expense paid or accrued pursuant to paragraph (g) of this section.

(iii) *Disallowance of addback.* No basis increase under paragraph (j)(5)(ii) of this section shall be allowed to upper-tier partnership for any disallowed UTP EBIE. For purposes of this section, the term disallowed UTP EBIE refers to any UTP EBIE that has a specified partner that is a transferee specified partner (as defined in paragraph (j)(8)(i) of this section) and any UTP EBIE that does not have a specified partner (as the result of a transaction described in paragraph (j)(6)(ii)(A) of this section). For purposes of applying paragraph (j)(5)(ii) of this section, upper-tier partnership shall treat any disallowed UTP EBIE in the same manner as UTP EBIE that has previously been allocated a negative section 734(b) adjustment and take such negative section 734(b) adjustment into account in the manner provided in paragraph (j)(7)(iv) of this section. However, upper-tier partnership does not treat disallowed UTP EBIE as though it were allocated a negative section 734(b) adjustment pursuant to this paragraph to the extent a negative section 734(b) or 743(b) adjustment was previously made to such disallowed UTP EBIE.

(9) *Determining allocable ATI and allocable business interest income of upper-tier partnership partners*—(i) *In general.* When applying paragraph (f)(2)(ii) of this section, an upper-tier partnership determines the allocable ATI and allocable business interest income of each of its partners in the manner provided in this paragraph. Specifically, if an upper-tier partnership's net amount of tax items that comprise (or have ever comprised) ATI is greater than or equal to its ATI, upper-tier partnership applies the rules in paragraph (j)(9)(ii)(A) of this section to determine each partner's allocable ATI. See *Example 32* in paragraph (o)(32) of this section. However, if an upper-tier partnership's net amount of tax items that comprise (or have ever comprised) ATI is less than its ATI, upper-tier partnership applies the rules in paragraph (j)(9)(ii)(B) of this section to determine each partner's allocable ATI. See *Example 33* in paragraph (o)(33) of this section. To determine each partner's allocable business interest income, an upper-tier partnership applies the rules in paragraph (j)(9)(iii) of this section.

(ii) *Upper-tier partner's allocable ATI*—(A) If an upper-tier partnership's net amount of tax items that comprise (or have ever comprised) ATI is greater than or equal to its ATI (as determined under § 1.163(j)–1(b)(1)), then an upper-tier partner's allocable ATI (for purposes of paragraph (f)(2)(ii) of this section) is equal to the product of—

(*1*) Such partner's distributive share of gross income and gain items that comprise (or have ever comprised) ATI, minus such partner's distributive share of gross loss and deduction items that comprise (or have ever comprised) ATI; multiplied by

(*2*) A fraction, the numerator of which is upper-tier partnership's ATI (as determined under § 163(j)–1(b)(1)), and the denominator of which is upper-tier partnership's net amount of tax items that comprise (or have ever comprised) ATI.

(B) If an upper-tier partnership's net amount of tax items that comprise (or have ever comprised) ATI is less than its ATI (as determined under § 1.163(j)–1(b)(1)), then an upper-tier partner's allocable ATI (for purposes of paragraph (f)(2)(ii) of this section) is equal to—

(*1*) The excess (if any) of such partner's distributive share of gross income and gain items that comprise (or have ever comprised) ATI, over such partner's distributive share of gross loss and deduction items that comprise (or have ever comprised) ATI; increased by

(*2*) The product of—

(*i*) Such partner's share of residual profits expressed as a fraction; multiplied by

(*ii*) Upper-tier partnership's ATI (as determined under § 1.163(j)–1(b)(1)), minus the aggregate of all the partners' amounts determined under paragraph (j)(9)(ii)(B)(*1*) of this section.

(iii) *Upper-tier partner's allocable business interest income.* An upper-tier partner's allocable business interest income (for purposes of paragraph (f)(2)(ii) of this section) is equal to the product of—

(A) Such partner's distributive share of items that comprise (or have ever comprised) business interest income; multiplied by

(B) A fraction, the numerator of which is upper-tier partnership's business interest income (as determined under § 1.163(j)–1(b)(4)), and the denominator of which is the upper-tier partnership's amount of items that comprise (or have ever comprised) business interest income.

* * * * *

(l) * * *

(4) * * *

(iv) *S corporation deductions capitalized by an S corporation shareholder.* The ATI of an S corporation shareholder is increased by the portion of such S corporation shareholder's allocable share of qualified expenditures (as defined in section 59(e)(2)) to which an election under section 59(e) applies.

* * * * *

(n) *Treatment of self-charged lending transactions between partnerships and partners.* In the case of a lending transaction between a partner (lending partner) and partnership (borrowing partnership) in which the lending partner owns a direct interest (self-charged lending transaction), any business interest expense of the borrowing partnership attributable to the self-charged lending transaction is business interest expense of the borrowing partnership for purposes of this section. If in a given taxable year the lending partner is allocated excess business interest expense from the borrowing partnership and has interest income attributable to the self-charged lending transaction (interest income), the lending partner is deemed to receive an allocation of excess business interest income from the borrowing partnership in such taxable year. The amount of the lending partner's deemed allocation of excess business interest income is the lesser of such lending partner's allocation of excess business interest expense from the borrowing partnership in such taxable year or the interest income attributable to the self-charged lending transaction in such taxable year. To prevent the double counting of business interest income, the lending partner includes interest income that was treated as excess business interest income pursuant to this paragraph (n) only once when calculating its own section 163(j) limitation. In cases where the lending partner is not a C corporation, to the extent that any interest income exceeds the lending partner's allocation of excess business interest expense from the borrowing partnership for the taxable year, and such interest income otherwise would be properly treated as investment income of the lending partner for purposes of section 163(d) for that year, such excess amount of interest income will continue to be treated as investment income of the lending partner for that year for purposes of section 163(d).

See *Example 26* in paragraph (o)(26) of this section.

(o) * * *

(24) *Example 24*—(i) *Facts.* On January 1, 2020, L and M form LM, a publicly traded partnership (as defined in § 1.7704–1), and agree that each will be allocated a 50 percent share of all LM items. The partnership agreement provides that LM will make allocations under section 704(c) using the remedial allocation method under § 1.704–3(d). L contributes depreciable property with an adjusted tax basis of $4,000 and a fair market value of $10,000. The property is depreciated using the straight-line method with a 10-year recovery period and has 4 years remaining on its recovery period. M contributes $10,000 in cash, which LM uses to purchase land. Except for the depreciation deductions, LM's expenses equal its income in each year of the 10 years commencing with the year LM is formed. LM has a valid section 754 election in effect.

(ii) *Section 163(j) remedial items and partner basis items.* LM sells the asset contributed by L in a fully taxable transaction at a time when the adjusted basis of the property is $4,000. Under § 1.163(j)–6(e)(2)(ii), solely for purposes of § 1.163(j)–6, the tax gain of $6,000 is allocated equally between L and M ($3,000 each). To avoid shifting built-in gain to the non-contributing partner (M) in a manner consistent with the rule in section 704(c), a remedial deduction of $3,000 is allocated to M (leaving M with no net tax gain), and remedial income of $3,000 is allocated to L (leaving L with total tax gain of $6,000).

(25) *Example 25*—(i) *Facts.* The facts are the same as *Example 24* in paragraph (o)(24) of this section except the property contributed by L had an adjusted tax basis of zero. For each of the 10 years following the contribution, there would be $500 of section 704(c) remedial income allocated to L and $500 of remedial deductions allocated to M with respect to the contributed asset. A buyer of M's units would step into M's shoes with respect to the $500 of annual remedial deductions. A buyer of L's units would step into L's shoes with respect to the $500 of annual remedial income and would have an annual section 743(b) deduction of $1,000 (net $500 of deductions).

(ii) *Analysis.* Pursuant to § 1.163(j)–6(d)(2)(ii), solely for purposes of § 1.163(j)–6, a buyer of L's units immediately after formation of LM would offset its $500 annual section 704(c) remedial income allocation with $500 of annual section 743(b) adjustment (leaving the buyer with net $500 of section 743(b) deduction). As a result, such buyer would be in the same position as a buyer of M's units. Each buyer would have net deductions of $500 per year, which would not affect ATI before 2022.

(26) *Example 26*—(i) *Facts.* X and Y are partners in partnership PRS. In Year 1, PRS had $200 of excess business interest expense. Pursuant to § 1.163(j)–6(f)(2), PRS allocated $100 of such excess business interest expense to each of its partners. In Year 2, X lends $10,000 to PRS and receives $1,000 of interest income for the taxable year (self-charged lending transaction). X is not in the trade or business of lending money. The $1,000 of interest expense resulting from this loan is allocable to PRS's trade or business assets. As a result, such $1,000 of interest expense is business interest expense of PRS. X and Y are each allocated $500 of such business interest expense as their distributive share of PRS's business interest expense for the taxable year. Additionally, in Year 2, PRS has $3,000 of ATI. PRS allocates the items comprising its $3,000 of ATI $0 to X and $3,000 to Y.

(ii) *Partnership-level.* In Year 2, PRS's section 163(j) limit is 30 percent of its ATI plus its business interest income, or $900 ($3,000 × 30 percent). Thus, PRS has $900 of deductible business interest expense, $100 of excess business interest expense, $0 of excess taxable income, and $0 of excess business interest income. Pursuant to § 1.163(j)–6(f)(2), $400 of X's allocation of business interest expense is treated as deductible business interest expense, $100 of X's allocation of business interest expense is treated as excess business interest expense, and $500 of Y's allocation of business interest expense is treated as deductible business interest expense.

(iii) *Lending partner.* Pursuant to § 1.163(j)–6(n), X treats $100 of its $1,000 of interest income as excess business interest income allocated from PRS in Year 2. Because X is deemed to have been allocated $100 of excess business interest income from PRS, and excess business interest expense from a partnership is treated as paid or accrued by a partner to the extent excess business interest income is allocated from such partnership to a partner, X treats its $100 allocation of excess business interest expense from PRS in Year 2 as business interest expense paid or accrued in Year 2. X, in computing its limit under section 163(j), has $100 of business interest income ($100 deemed allocation of excess business interest income from PRS in Year 2) and $100 of business interest expense ($100 allocation of excess business interest expense treated as paid or accrued in Year 2). Thus, X's $100 of business interest expense is deductible business interest expense. At the end of Year 2, X has $100 of excess business interest expense from PRS ($100 from Year 1). X treats $900 of its $1,000 of interest income as investment income for purposes of section 163(d).

(27) *Example 27*—(i) *Formation.* A, B, and C formed partnership UTP in Year 1, each contributing $1,000 cash in exchange for a one third interest. Also in Year 1, UTP, D, and E formed partnership LTP, each contributing $1,200 cash in exchange for a one third interest. LTP borrowed $9,000, resulting in each of its partners increasing its basis in LTP by $3,000. Further, the partners of UTP each increased their bases in UTP by $1,000 each as a result of the LTP borrowing.

(ii) *Application of section 163(j) to LTP.* In Year 1, LTP's only item of income, gain, loss, or deduction was $900 of BIE. As a result, LTP had $900 of excess business interest expense. Pursuant to § 1.163(j)–6(f)(2), LTP allocated $300 of excess business interest expense to each of its partners.

(iii) *Section 704(b) capital account adjustments.* Solely for purposes of section 704(b) and the regulations thereunder, each direct and indirect partner of LTP treats its allocation of excess business interest expense from LTP as a section 705(a)(2)(B) expenditure pursuant to § 1.163(j)–6(j)(2). Further, each indirect partner of LTP that reduced its section 704(b) capital account as a result of the $300 allocation of excess business interest expense to UTP is the specified partner of such UTP EBIE, as defined in § 1.163(j)–6(j)(5)(i)(B). Each partner of UTP reduced its capital account by $100 as a result of the $300 allocation of excess business interest expense from LTP to

UTP. As a result, A, B, and C are each a specified partner with respect to $100 of UTP EBIE.

(iv) *Basis adjustments.* Pursuant to § 1.163(j)–6(h)(2), D, E, and UTP each reduce its basis in LTP by the amount of its allocation of excess business interest expense from LTP. As a result, each partner's basis in its LTP interest is $3,900. Pursuant to § 1.163(j)–6(j)(3), the direct partners of UTP (A, B, and C) do not reduce the bases of their interests in UTP as a result of the allocation of excess business interest expense from LTP to UTP. UTP treats its $300 allocation of excess business interest expense from LTP as UTP EBIE, as defined in § 1.163(j)–6(j)(4). At the end of Year 1, the section 704(b) and tax basis balance sheets of LTP and UTP are as follows:

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Table 60 to paragraph (o)(27)(iv)--UTP Balance Sheet - End of Year 1

	Assets			Liabilities and Capital		
	Tax	Book		Tax	Book	
Cash	$1,800	$1,800	Liability	$3,000	$3,000	
LTP	3,900	3,900	Capital:			Basis
UTP EBIE	300	0	A	1,000	900	$2,000
			B	1,000	900	2,000
			C	1,000	900	2,000
Total	6,000	5,700	Total	6,000	5,700	6,000

Table 61 to paragraph (o)(27)(iv)--LTP Balance Sheet - End of Year 1

	Assets			Liabilities and Capital		
	Tax	Book		Tax	Book	
Cash	$11,700	$11,700	Liability	$9,000	$9,000	
			Capital:			Basis
			D	900	900	$3,900
			E	900	900	3,900
			UTP	900	900	3,900
Total	11,700	11,700	Total	11,700	11,700	11,700

Table 62 to paragraph (o)(27)(iv)--UTP EBIE - End of Year 1

	Specified partner			Partnership	
	Basis	Carryforward		Basis	Carryforward
A	$100	$100	UTP	$300	$300
B	100	100			
C	100	100			
Total	300	300	Total	300	300

(28) *Example 28*—(i) *Facts.* The facts are the same as *Example 27* in paragraph (o)(27) of this section. In Year 2, while a section 754 election was in effect, C sold its UTP interest to D for $900. In Year 3, LTP's only item of income, gain, loss, or deduction was $240 of income, which it allocated to UTP. Such $240 of income resulted in $240 of excess taxable income, which LTP allocated to UTP pursuant to § 1.163(j)–f(2). Further, in Year 3, UTP's only item of income, gain, loss, or deduction was its $240 allocation of income from LTP. UTP allocated such $240 of income equally among its partners. In Year 4, UTP sold its interest in LTP to X for $1,140.

(ii) *Sale of specified partner's UTP interest.* C's section 741 loss recognized on the sale of its partnership interest to D in Year 2 is $100 (amount realized of $900 cash, plus $1,000 relief of liabilities, less $2,000 basis in UTP). D's initial adjusted basis in the UTP interest acquired from C in Year 2 is $1,900 (the cash paid for C's interest, $900, plus $1,000, D's share of UTP liabilities). D's interest in UTP's previously taxed capital is $1,000 ($900, the amount of cash D would receive if PRS liquidated immediately after the hypothetical transaction, decreased by $0, the amount of tax gain allocated to D from the hypothetical transaction, and increased by $100, the amount of tax loss that would be allocated to D from the hypothetical transaction). D's share of the adjusted basis to the partnership of the partnership's property is $2,000 ($1,000 share of previously taxed capital, plus $1,000 share of the partnership's liabilities). Therefore, the amount of the basis adjustment under section 743(b) to partnership property is negative $100 (the difference between $1,900 and $2,000). D's negative $100 section 743(b) adjustment is allocated among UTP's assets under section 755. Under § 1.755–1(b)(2), the amount of D's section 743(b) adjustment allocated to ordinary income property is equal to the total amount of income or loss that would be allocated to D from the sale of all ordinary income property in a hypothetical transaction. Solely for purposes of § 1.755–1(b), any UTP EBIE is treated as ordinary income property. Thus, D's negative $100 section 743(b) basis adjustment is allocated to UTP EBIE.

(iii) *Application of section 163(j) to UTP.* In Year 3, UTP was allocated excess taxable income from LTP. Thus, UTP applies the rules in § 1.163(j)–6(j)(5)(i). First, pursuant to § 1.163(j)–6(j)(5)(i)(A), UTP applies the rules in § 1.163(j)–6(g) to its UTP EBIE. Because UTP was allocated $240 of excess taxable income from LTP in Year 3, UTP treats $240 of its UTP EBIE as business interest expense paid or accrued in Year 3. Specifically, UTP treats $80 of each partner's share of UTP EBIE as business interest expense paid or accrued. Under these circumstances, UTP's method for determining which UTP EBIE is treated as business interest expense paid or accrued is reasonable. Second, pursuant to § 1.163(j)–6(j)(5)(i)(B), UTP allocates such business interest expense that was formerly UTP EBIE to its specified partner. Accordingly, A and B are each allocated $80 of business interest expense. Pursuant to § 1.163(j)–6(j)(6)(i), D is treated as the specified partner with respect to $100 of UTP EBIE (C's share of UTP EBIE prior to the sale). Further, pursuant to § 1.163(j)–6(j)(5)(i)(A), $80 of the UTP EBIE to which D is the specified partner was treated as business interest expense paid or accrued. Accordingly, D is allocated such $80 of business interest expense. After determining each partner's allocable share of section 163(j) items used in its own section 163(j) calculation, UTP determines each partner's allocable share of excess items pursuant to § 1.163(j)–6(f)(2).

TABLE 62 TO PARAGRAPH (o)(28)(iii)—UTP'S APPLICATION OF § 1.163(j)–6(f)(2)(II) IN YEAR 3

	A	B	D	Total
Allocable ATI	$80	$80	$80	$240
Allocable BII	0	0	0	0
Allocable BIE	80	80	80	240

TABLE 63 TO PARAGRAPH (o)(28)(iii)—UTP'S APPLICATION OF § 1.163(j)–6(f)(2)(xi) IN YEAR 3

	A	B	D	Total
Deductible BIE	$24	$24	$24	$72
EBIE allocated	56	56	56	168
ETI allocated	0	0	0	0
EBII allocated	0	0	0	0

(iv) *Treatment of business interest expense that was formerly UTP EBIE.* After determining each partner's share of deductible business interest expense and section 163(j) excess items, UTP takes into account any basis adjustments under section 734(b) and the partners take into account any basis adjustments under section 743(b) to business interest expense that was formerly UTP EBIE pursuant to § 1.163(j)–6(j)(5)(i)(C). None of the UTP EBIE treated as business interest expense paid or accrued in Year 3 was allocated a section 734(b) adjustment. Additionally, neither A's nor B's share of business interest expense that was formerly UTP EBIE was allocated a section 743(b) basis adjustment. Further, neither A nor B is a transferee specified partner, as defined in § 1.163(j)–6(j)(8)(i). Therefore, no special adjustments are required to A's or B's $24 of deductible business interest expense and $56 of excess business interest expense. At the end of Year 3, A and B each has an adjusted basis in UTP of $2,000 and each is the specified partner with respect to $20 of UTP EBIE. D's share of business interest expense that was formerly UTP EBIE was allocated a negative $80 section 743(b) adjustment. Pursuant to § 1.163(j)–6(j)(7)(ii), D recovers $24 of the negative section 743(b) adjustment, effectively eliminating the $24 deduction resulting from its $24 allocation of deductible business interest expense. Additionally, pursuant to § 1.163(j)–6(j)(7)(iii), the $56 basis decrease required under § 1.163(j)–6(h)(2) for D's allocation of excess business interest expense is reduced by the negative section 743(b) adjustment attributable to such excess business interest expense ($56). Consequently, D does not reduce the basis of its interest in UTP pursuant § 1.163(j)–6(h)(2) upon being allocated such excess business interest expense. As a result, D has $56 of excess business interest expense with a basis of $0. At the end of Year 3, D has an adjusted basis in UTP of $1,980 and is the specified partner with respect to $20 of UTP EBIE.

(v) *Application of anti-loss trafficking rules.* Although D is a transferee specified partner, as defined in § 1.163(j)–6(j)(8)(i), with respect to its $80 allocation of business interest expense from UTP, no special basis adjustments under § 1.163(j)–6(j)(8)(i) are required because all $80 of such business interest expense was already fully offset by negative section 743(b) adjustment. However, if such $80 of business interest expense was not fully offset by a negative section 743(b) adjustment, D's status as transferee specified partner would cause such business interest expense to be fully offset by a negative section 743(b) adjustment pursuant to § 1.163(j)–6(j)(8)(i), regardless of whether a section 754 election was not in effect with respect to the sale of UTP from C to D. Such negative section 743(b) adjustment would be taken into account in the manner described in § 1.163(j)–6(j)(7).

Table 64 to paragraph (o)(28)(v)--UTP EBIE - End of Year 3

	Specified partner				Partnership	
	Basis	743(b)	Carryforward		Basis	Carryforward
A	$20		$20	UTP	$60	$60
B	20		20			
D	20	(20)	20			
Total	60		60	Total	60	60

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(vi) *Sale of LTP interest.* In Year 4, UTP disposed of its interest in LTP. Thus, UTP applies the rules in § 1.163(j)–6(j)(5)(ii). First, pursuant to § 1.163(j)–6(j)(5)(ii)(A), UTP applies the rules in § 1.163(j)–6(h)(3) to its UTP EBIE. Because UTP disposed of all of its LTP interest, UTP reduces its UTP EBIE by $60. Second, pursuant to § 1.163(j)–6(j)(5)(ii)(B), UTP increases the adjusted basis of its LTP interest by $60 (the total amount of UTP EBIE that was reduced pursuant to § 1.163(j)–6(j)(5)(ii)(A)). Third, pursuant to § 1.163(j)–6(j)(5)(ii)(C), this $60 increase is reduced by $20 to take into account the negative $20 section 743(b) adjustment allocated in Year 2 to the $20 of UTP EBIE reduced pursuant to § 1.163(j)–6(j)(5)(ii)(A). As a result, UTP's adjusted basis in its LTP interest immediately prior to the sale to X is $4,180 ($3,900 at the end of Year 1, plus $240 allocation of income from LTP in Year 3, plus $40 increase immediately prior to the sale attributable to the basis of UTP EBIE). UTP's section 741 loss recognized on the sale is $40 (amount realized of $1,140 cash, plus $3,000 relief of liabilities, less $4,180 adjusted basis in LTP). No deduction under section 163(j) is allowed to the UTP or X under chapter 1 of subtitle A of the Code for any of such UTP EBIE reduced under § 1.163(j)–6(h)(3). Pursuant to § 1.163(j)–6(h)(5), LTP has a § 1.163(j)–6(h)(5) basis adjustment of $40. LTP does not own property of the character required to be adjusted. Thus, under § 1.755–1(c)(4), the adjustment is made when LTP subsequently acquires capital gain property to which an adjustment can be made. Regardless of whether a $20 negative section 743(b) adjustment was allocated to the $20 of UTP EBIE reduced pursuant to § 1.163(j)–6(j)(5)(ii)(A), UTP would only increase its basis in LTP pursuant to § 1.163(j)–6(j)(5)(ii) by $40. The specified partner of such $20 of UTP EBIE is a transferee specified partner. Therefore, it is treated as disallowed UTP EBIE under § 1.163(j)–6(j)(8)(iii) of this section. As a result, UTP would treat such $20 of UTP EBIE for purposes of § 1.163(j)–6(j)(5)(ii) as though it were allocated a negative section 734(b) adjustment of $20.

(29) *Example 29*—(i) *Facts.* The facts are the same as *Example 27* in paragraph (o)(27) of this section. In Year 2, while a section 754 election was in effect, UTP distributed $900 to C in complete liquidation of C's partnership interest. In Year 3, LTP's only item of income, gain, loss, or deduction was $240 of income, which it allocated to UTP. Such $240 of income resulted in $240 of excess taxable income, which LTP allocated to UTP pursuant to § 1.163(j)–f(2). Further, in Year 3, UTP's only item of income, gain, loss, or deduction was its $240 allocation of income from LTP. UTP allocated such $240 of income equally among its partners. In Year 4, UTP sold its interest in LTP to X for $1,140.

(ii) *Liquidating distribution to specified partner.* C's section 731(a)(2) loss recognized on the disposition of its partnership interest is $100 ($2,000 basis in UTP, less amount realized of $900 cash, plus $1,000 relief of liabilities). Because the election under section 754 is in effect, UTP has a section 734(b) decrease to the basis of its assets of $100 (the amount of section 731(a)(2) loss recognized by C). Under section 755, the entire negative $100 section 734(b) adjustment is allocated to UTP EBIE. Following the liquidation of C, UTP's basis in its assets ($900 of cash, plus $3,900 interest in LTP, plus $200 basis of UTP EBIE) equals the aggregate outside basis of partners A and B ($5,000).

(iii) *Application of section 163(j) to UTP.* In Year 3, UTP was allocated excess taxable income from LTP. Thus, UTP applies the rules in § 1.163(j)–6(j)(5)(i). First, pursuant to § 1.163(j)–6(j)(5)(i)(A), UTP applies the rules in § 1.163(j)–6(g) to its UTP EBIE. Because UTP was allocated $240 of excess taxable income from LTP in Year 3, UTP treats $240 of its UTP EBIE as business interest expense paid or accrued in Year 3. Specifically, UTP treats $100 of A's share, $100 of B's share, and $40 of the UTP EBIE that does not have a specified partner as business interest expense paid or accrued. Under these circumstances, UTP's method for determining which UTP EBIE is treated as business interest expense paid or accrued is reasonable. Second, pursuant to § 1.163(j)–6(j)(5)(i)(B), UTP allocates such business interest expense that was formerly UTP EBIE to its specified partner. Accordingly, each of A and B is allocated $100 of business interest expense.

(iv) *Application of anti-loss trafficking rules.* Following the liquidating distribution to C in Year 2 (a transaction described in § 1.163(j)–6(j)(6)(ii)(A)), the $100 of UTP EBIE to which C was formerly the specified partner does not have a specified partner. Thus, UTP does not allocate any deductible business interest expense or excess business interest expense that was formerly C's share of UTP EBIE to A or B. Rather, pursuant to § 1.163(j)–6(j)(8)(ii), UTP treats such business interest expense as the allocable business interest expense, as defined in § 1.163(j)–6(f)(2)(ii), of a § 1.163(j)–6(j)(8)(ii) account for purposes of applying § 1.163(j)–6(f)(2). After determining each partner's allocable share of section 163(j) items used in its own section 163(j) calculation, UTP determines each partner's allocable share of excess items pursuant to § 1.163(j)–6(f)(2).

TABLE 65 TO PARAGRAPH (o)(29)(iv)—UTP'S APPLICATION OF § 1.163(j)–6(f)(2)(ii) IN YEAR 3

	A	B	§ 1.163(j)–6(j)(8)(ii) account	Total
Allocable ATI	$120	$120	$0	$240
Allocable BII	0	0	0	0
Allocable BIE	100	100	40	240

TABLE 65 TO PARAGRAPH (o)(29)(iv)—UTP'S APPLICATION OF § 1.163(j)–6(f)(2)(xi) IN YEAR 3

	A	B	§ 1.163(j)–6(j)(8)(ii) account	Total
Deductible BIE	$36	$36	$0	$72
EBIE allocated	64	64	40	168
ETI allocated	0	0	0	0
EBII allocated	0	0	0	0

(v) *Treatment of business interest expense that was formerly UTP EBIE.* After determining each partner's share of deductible business interest expense and section 163(j) excess items, UTP takes into account any basis adjustments under section 734(b) and the partners take into account any basis under section 743(b) to business interest expense that was formerly UTP EBIE pursuant to § 1.163(j)–6(j)(5)(i)(C). None of the UTP EBIE treated as business interest expense paid or accrued in Year 3 was allocated a section 743(b) adjustment. Further, neither A nor B is a transferee specified partner, as defined in § 1.163(j)–6(j)(8)(i). Therefore, no special basis adjustments are required under § 1.163(j)–6(j)(8)(i). The $40 of excess business interest expense allocated to the § 1.163(j)–6(j)(8)(ii) account is not allocated to A or B and is not carried over by UTP. Additionally, UTP does not have a § 1.163(j)–6(h)(5) basis adjustment because such $40 of business interest expense does not have any basis. Thus, A and B each has $36 of deductible business interest expense and $64 of excess business interest expense. At the end of Year 3, A and B each has an adjusted basis in UTP of $2,520 ($2,500 outside basis, plus $120 allocation of income, less $36 of deductible business interest expense, less $64 of excess business interest expense), and neither A nor B is a specified partner with respect to any of UTP's $60 of UTP EBIE.

TABLE 66 TO PARAGRAPH (o)(29)(v)—UTP EBIE—END OF YEAR 3

	Specified partner			Partnership	
	Basis	Carryforward		Basis	Carryforward
A	$0	$0	UTP	$0	$60
B	0	0			
§ 1.163(j)–6(j)(8)(ii) account	0	60			
Total	0	60	Total	0	60

(vi) *Sale of LTP interest.* In Year 4, UTP disposed of its interest in LTP. Thus, UTP applies the rules in § 1.163(j)–6(j)(5)(ii). First, pursuant to § 1.163(j)–6(j)(5)(ii)(A), UTP applies the rules in § 1.163(j)–6(h)(3) to its UTP EBIE. Because UTP disposed of all of its LTP interest, UTP reduces its UTP EBIE by $60. Second, pursuant to § 1.163(j)–6(j)(5)(ii)(B), UTP increases the adjusted basis of its LTP interest by $60 (the total amount of UTP EBIE that was reduced pursuant to § 1.163(j)–6(j)(5)(ii)(A)). Third, pursuant to § 1.163(j)–6(j)(5)(ii)(C), this $60 increase is reduced by $60 to take into account the negative $60 section 734(b) adjustment allocated in Year 2 to the $60 of UTP EBIE reduced pursuant to § 1.163(j)–6(j)(5)(ii)(A). As a result, UTP's adjusted basis in its LTP interest immediately prior to the sale to X is $4,140 ($3,900 at the end of Year 1, plus $240 allocation of income from LTP in Year 3). UTP has no section 741 gain or loss recognized on the sale (amount realized of $1,140 cash, plus $3,000 relief of liabilities, equals $4,140 adjusted basis in LTP). No deduction under section 163(j) is allowed to the UTP or X under chapter 1 of subtitle A of the Code for any of such UTP EBIE reduced under § 1.163(j)–6(h)(3). Regardless of whether the $60 of UTP EBIE's basis was reduced by a $60 negative section 734(b) adjustment, UTP would not increase its basis in LTP pursuant to § 1.163(j)–6(j)(5)(ii) of this section as a result of the sale to X. The $60 of UTP EBIE does not have a specified partner. Therefore, it is treated as disallowed UTP EBIE under § 1.163(j)–6(j)(8)(iii) of this section. As a result, UTP would treat such $60 of UTP EBIE for purposes of § 1.163(j)–6(j)(5)(ii) as though it were allocated a negative section 734(b) adjustment of $60.

(30) *Example 30*—(i) X, Y and Z are partners in partnership PRS, PRS and A are partners in UTP, and UTP is a partner in LTP. LTP allocates $15 of excess business interest expense to UTP. Pursuant to § 1.163(j)–6(j)(2), UTP reduces its section 704(b) capital account (capital account) in LTP by $15, A reduces its capital account in UTP by $5, PRS reduces its capital account in UTP by $10, X reduces its capital account in PRS by $4, and Y reduces its capital account in PRS by $6. Thus, A, PRS, X, and Y are the specified partner with respect to $5, $10, $4, and $6 of UTP EBIE, respectively.

(ii) Assume the same facts in (i) except that PRS distributed cash to Y in complete liquidation of Y's interest in PRS. As a result, pursuant to § 1.163(j)–6(j)(6)(ii)(A), Y's share of UTP EBIE would not have a specified partner. In a subsequent year, if LTP allocated UTP $15 of excess business interest income, UTP would apply the rules in § 1.163(j)–6(j)(5)(i) and allocate $5 of deductible business interest expense to A and $10 of deductible business interest expense to PRS (the specified partners of such deductible business interest expense). Because the $10 of deductible business interest expense allocated to PRS was formerly UTP EBIE, PRS must also apply the rules in § 1.163(j)–6(j)(5)(i). PRS would allocate $4 of such deductible business interest expense to X (the specified partner of such $4). However, as a result of the liquidating distribution to Y, the remaining $6 of deductible business interest expense does not have a specified partner. Thus, pursuant to § 1.163(j)–6(j)(8)(ii), PRS would make a § 1.163(j)–6(h)(5) basis adjustment to its property in the amount of the adjusted basis (if any) of such $6 of deductible business interest expense.

(iii) Assume the same facts as in (i) except that PRS distributed its interest in UTP to Y in complete liquidation of Y's interest in PRS. Pursuant to § 1.163(j)–6(j)(6)(ii)(A), Y is the specified partner with respect to UTP EBIE of UTP only to the same extent it was prior to the distribution ($6). As a result, the UTP EBIE of UTP in excess of the UTP EBIE for which Y is the specified partner (X's $4) does not have a specified partner. If in a subsequent year LTP allocated UTP $15 of excess business interest income, UTP would apply the rules in § 1.163(j)–6(j)(5)(i) and allocate $5 of deductible business interest expense to A and $6 of deductible business interest expense to Y. Regarding the $4 of DBIE without a specified partner, UTP would apply the rules in § 1.163(j)–6(j)(8)(ii) and make a § 1.163(j)–6(h)(5) basis adjustment to its property in the amount of the adjusted basis (if any) of such $4 of deductible business interest expense.

(iv) Assume the same facts as in (i) except that A contributes its UTP interest to a new partnership, PRS2. Following the contribution, PRS2 is treated as the specified partner with respect to the portion of the UTP EBIE attributable to the contributed interest ($5). Further, A continues to be the specified partner with respect to the UTP EBIE attributable to the contributed interest ($5). If in a subsequent year LTP allocated UTP $15 of excess business interest income, UTP would apply the rules in § 1.163(j)–6(j)(5)(i) and allocate $5 of deductible business interest expense to PRS2, and PRS2 would allocate such $5 of deductible business interest expense to A.

(31) *Example 31*—(i) *Facts.* In Year 1, A, B, and C formed partnership PRS by each contributing $1,000 cash. PRS borrowed $900, causing each partner's basis in PRS to increase by $300 under section 752. Also in Year 1, PRS purchased Capital Asset X for $200. In Year 2, PRS pays $300 of business interest expense, all of which is disallowed and treated as excess business interest expense. PRS allocated the $300 of excess business interest expense to its partners, $100 each. Pursuant to § 1.163(j)–6(h)(2), each partner reduced its adjusted basis in its PRS interest by its $100 allocation of excess business interest expense to $1,200. In Year 3, when the fair market value of Capital Asset X is $3,200 and no partner's basis in PRS has changed, PRS distributed $1,900 to C in complete liquidation of C's partnership interest in a distribution to which section 737 does not apply. PRS had a section 754 election in effect in Year 3.

(ii) *Consequences to selling partner.* Pursuant to § 1.163(j)–6(h)(3), C increases the adjusted basis of its interest in PRS by $100 immediately before the disposition. Thus, C's section 731(a)(1) gain recognized on the disposition of its interest in PRS is $900 (($1,900 cash + $300 relief of liabilities) − ($1,200 outside basis + $100 excess business interest expense add-back)).

(iii) *Partnership basis.* Pursuant to § 1.163(j)–6(h)(5), PRS has a $100 increase to the basis of its assets attributable to a § 1.163(j)–6(h)(5) basis increase immediately before C's disposition. Under section 755, the entire $100 adjustment is allocated to Capital Asset X. Pursuant to § 1.163(j)–6(h)(5), regardless of whether Capital Asset X is a depreciable or amortizable asset, none of the $100 of § 1.163(j)–6(h)(5) basis increase allocated to Capital Asset X is depreciable or amortizable. Additionally, PRS has a section 734(b) increase to the basis of its assets of $900 (the amount of section 731(a)(1) gain recognized by C). Under section 755, the entire $900 adjustment is allocated to Capital Asset X. As a result, PRS's basis in Capital Asset X is $1,200 ($200 + $100 § 1.163(j)–6(h)(5) basis increase + $900 section 734(b) adjustment). Following the liquidation of C, PRS's basis in its assets ($600 cash + $1,200

Capital Asset X) equals the aggregate adjusted basis of partners A and B in PRS ($1,800).

(32) *Example 32*—(i) *Facts.* X and Y are equal partners in partnership UTP, which is a partner in partnership LTP. In Year 1, LTP allocated $100 of income to UTP. LTP, in computing its limit under section 163(j), treated such $100 of income as ATI. Accordingly, in LTP's § 1.163(j)–6(f)(2)(ii) calculation, UTP's allocable ATI was $100. Additionally, pursuant to § 1.163(j)–6(f)(2), LTP allocated $50 of excess taxable income to UTP. UTP's only items of income, gain, loss or deduction in Year 1, other than the $100 allocation from LTP, were $100 of trade or business income and $30 of business interest expense. UTP allocated its $200 of income and gain items $100 to X and $100 to Y, and all $30 of its business interest expense to X.

(ii) *Partnership-level.* Pursuant to § 1.163(j)–6(e)(1), UTP, in computing its limit under section 163(j), does not increase or decrease any of its section 163(j) items by any of LTP's section 163(j) items. Pursuant to § 1.163(j)–1(b)(1), UTP determines it has $150 of ATI in Year 1 ($100 of ATI resulting from its $100 of trade or business income, plus $50 of excess taxable income from LTP). UTP's section 163(j) limit is 30 percent of its ATI, or $45 ($150 × 30 percent). Thus, UTP has $50 of excess taxable income and $30 of deductible business interest expense.

(iii) *Partner-level allocations.* UTP allocates its $50 of excess taxable income and $30 of deductible business interest expense to X and Y pursuant to § 1.163(j)–6(f)(2). To determine each partner's share of the $50 of excess taxable income, UTP must determine each partner's allocable ATI and allocable business interest expense (as defined in § 1.163(j)–6(f)(2)(ii)). X's allocable business interest expense is $30 and Y's allocable business interest expense is $0. Because UTP is an upper-tier partnership, UTP determines the allocable ATI of each of its partners in the manner provided in § 1.163(j)–6(j)(9). Specifically, because UTP's net amount of tax items that comprise (or have ever comprised) ATI is $200 ($100 of trade or business income that UTP treated as ATI, plus UTP's $100 allocation from LTP of items that comprised ATI to LTP), which is greater than its $150 of ATI, UTP must apply the rules in § 1.163(j)–6(j)(9)(ii)(A) to determine each of its partner's allocable ATI. UTP determines X's allocable ATI is $75 (X's $100 distributive share of gross income and gain items that comprise (or have ever comprised) ATI, multiplied by ($150/$200), the ratio of UTP's ATI to its tax items that comprise (or have ever comprised) ATI). In a similar manner, UTP determines Y's allocable ATI also equals $75. Therefore, pursuant to § 1.163(j)–6(f)(2), X is allocated $30 of deductible business interest expense and Y is allocated $50 of excess taxable income.

(33) *Example 33*—(i) *Facts.* X and Y are equal partners in partnership UTP, which is a partner in partnership LTP. Further, X and Y share the residual profits of UTP equally. In Year 1, LTP allocated ($99) of income to UTP. LTP, in computing its limit under section 163(j), treated such ($99) of income as ATI. Accordingly, in LTP's § 1.163(j)–6(f)(2)(ii) calculation, UTP's allocable ATI was ($99). UTP's only items of income, gain, loss or deduction in Year 1, other than the ($99) allocation from LTP, were $100 of trade or business income and $15 of business interest expense. UTP allocated $1 of income to X and $0 to Y pursuant to section 704(c), the ($99) of loss and remaining $99 of income equally pursuant to section 704(b), and all $15 of its business interest expense to X.

(ii) *Partnership-level.* Pursuant to § 1.163(j)–6(e)(1), UTP, in computing its limit under section 163(j), does not increase or decrease any of its section 163(j) items by any of LTP's section 163(j) items. Pursuant to § 1.163(j)–1(b)(1), UTP determines it has $100 of ATI in Year 1 ($100 of ATI resulting from its $100 of trade or business income). UTP's section 163(j) limit is 30 percent of its ATI, or $30 ($100 × 30 percent). Thus, UTP has $50 of excess taxable income and $15 of deductible business interest expense.

(iii) *Partner-level allocations.* UTP allocates its $50 of excess taxable income and $15 of deductible business interest expense to X and Y pursuant to § 1.163(j)–6(f)(2). To determine each partner's share of the $50 of excess taxable income, UTP must determine each partner's allocable ATI and allocable business interest expense (as defined in § 1.163(j)–6(f)(2)(ii)). X's allocable business interest expense is $15 and Y's allocable business interest expense is $0. Because UTP is an upper-tier partnership, UTP determines the allocable ATI of each of its partners in the manner provided in § 1.163(j)–6(j)(9). Specifically, because UTP's net amount of tax items that comprise (or have ever comprised) ATI is $1 ($100 of trade or business income that UTP treated as ATI, plus UTP's ($99) allocation from LTP of items that comprised ATI to LTP), which is less than its $100 of ATI, UTP must apply the rules in § 1.163(j)–6(j)(9)(ii)(B) to determine each of its partner's allocable ATI. UTP determines X's allocable ATI is $50.50 ($1, which is the excess of X's distributive share of gross income and gain items that comprise (or have ever comprised) ATI, $100, over X's distributive share of gross loss and deduction items that comprise (or have ever comprised) ATI, $99; increased by $49.50, which is the product of 50 percent, X's residual profit sharing percentage, and $99, UTP's $100 of ATI minus $1, which is the aggregate of all the partners' amounts determined under § 1.163(j)–6(j)(9)(ii)(B)(*1*)). In a similar manner, UTP determines Y's allocable ATI is $49.50. Therefore, pursuant to § 1.163(j)–6(f)(2), X is allocated $15 of deductible business interest expense and $0.50 of excess taxable income, and Y is allocated $49.50 of excess taxable income.

(34) *Example 34*—(i) *Facts.* X and Y are equal partners in partnership PRS. Further, X and Y share the profits of PRS equally. In 2019, PRS had ATI of $100. In 2020, PRS's only items of income, gain, loss or deduction was $1 of trade or business income, which it allocated to X pursuant to section 704(c).

(ii) *Partnership-level.* In 2020, PRS makes the election described in § 1.163(j)–6(d)(5) to use its 2019 ATI in 2020. As a result, PRS has $100 of ATI in 2020. PRS does not have any business interest expense. Therefore, PRS has $100 of excess taxable income in 2020.

(iii) *Partner-level allocations.* PRS allocates its $100 of excess taxable income to X and Y pursuant to § 1.163(j)–6(f)(2). To determine each partner's share of the $100 of excess taxable income, PRS must determine each partner's allocable ATI (as defined in § 1.163(j)–6(f)(2)(ii)). Because PRS made the election described in § 1.163(j)–6(d)(5), PRS must determine the allocable ATI of each of its partners pursuant to paragraph (j)(9) of this section in the same manner as an upper-tier partnership. Specifically, because PRS's amount of tax items that comprise ATI before the election is $1, which is less than its $100 of ATI following the election, PRS must apply the rules in § 1.163(j)–6(j)(9)(ii)(B) to determine each of its partner's allocable ATI. PRS determines X's allocable ATI is $50.50 ($1, which is the excess of X's distributive share of gross income and gain items that would have comprised ATI had PRS not made the election, $1, over X's distributive share of gross loss and deduction items that would have comprised ATI had PRS not made the election, $0; increased by $49.50, which is the product of 50%, X's residual profit share, and $99, PRS's $100 of ATI minus $1, the aggregate of all the partners' amounts determined under § 1.163(j)–6(j)(9)(ii)(B)(*1*)). In a similar manner, PRS determines Y's allocable ATI is $49.50. Therefore, pursuant to § 1.163(j)–6(f)(2), X is allocated $50.50 of excess taxable income, and Y is allocated $49.50 of excess taxable income.

(35) *Example 35*—(i) *Facts.* X, a partner in partnership PRS, was allocated $20 of excess business interest expense from PRS in 2018 and $10 of excess business interest expense from PRS in 2019. In 2020, PRS allocated $16 of excess taxable income to X.

(ii) *Analysis.* X treats 50 percent of its $10 of excess business interest expense allocated from PRS in 2019 as § 1.163(j)–6(g)(4) business interest expense. Thus, $5 of § 1.163(j)–6(g)(4) business interest expense is treated as paid or accrued by X in 2020 and is not subject to the section 163(j) limitation at X's level. Because X was allocated $16 of excess taxable income from PRS in 2020, X treats $16 of its $25 of excess business interest expense as business interest expense paid or accrued pursuant to § 1.163(j)–6(g)(2). X, in computing its limit under section 163(j) in 2020, has $16 of ATI (as a result of its allocation of $16 of excess taxable income from PRS), $0 of business interest income, and $16 of business interest expense ($16 of excess business interest expense treated as paid or accrued in 2020). Pursuant to § 1.163(j)–2(b)(2)(i), X's section 163(j) limit in 2020 is $8 ($16 × 50 percent). Thus, X has $8 of business interest expense that is deductible under section 163(j). The $8 of X's business interest expense not allowed as a deduction ($16 business interest expense subject to section 163(j), less $8 section 163(j) limit) is treated as business interest expense paid or accrued by X in 2021. At the end of 2020, X has $9 of excess business interest expense from PRS ($20 from 2018, plus $10 from 2019, less $5 treated as paid or accrued pursuant to § 1.163(j)–6(g)(4), less $16 treated as paid or accrued pursuant to § 1.163(j)–6(g)(2)).

(36) *Example 36*—(i) *Facts.* X is a partner in partnership PRS. At the beginning of 2018, X's outside basis in PRS was $100. X was

allocated $20 of excess business interest expense from PRS in 2018 and $10 of excess business interest expense from PRS in 2019. X sold its PRS interest in 2019 for $70.

(ii) *Analysis.* X treats 50 percent of its $10 of excess business interest expense allocated from PRS in 2019 as § 1.163(j)–6(g)(4) business interest expense. Thus, $5 of § 1.163(j)–6(g)(4) business interest expense is treated as paid or accrued by X in 2020 and is not subject to the section 163(j) limitation at X's level. Pursuant to paragraph (h)(3) of this section, immediately before the disposition, X increases the basis of its PRS interest to $95. Thus, X has a $25 section 741 loss recognized on the sale ($70–$95).

(p) *Applicability dates*—(1) *In general.*

* * *

(2) *Paragraphs (c)(1) and (2), (d)(3) through (5), (e)(5) and (6), (f)(1)(iii), (g)(4), (h)(4) and (5), (j), (l)(4)(iv), (n), and (o)(24) through (29).* Paragraphs (c)(1) and (2), (d)(3) through (5), (e)(5) and (6), (f)(1)(iii), (g)(4), (h)(4) and (5), (j), (l)(4)(iv), (n), and (o)(24) through (29) of this section apply to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of those paragraphs to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], provided that they also apply the provisions of § 1.163(j)–6 in the section 163(j) regulations, and consistently apply all of the rules of § 1.163(j)–6 in the section 163(j) regulations to that taxable year and to each subsequent taxable year.

* * * * *

■ **Par. 8.** As added in a final rule elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.163(j)–7 is amended by revising paragraph (a), adding paragraphs (c) through (f), (g)(3) and (4), (h), and (j) through (l), and revising paragraph (m) to read as follows:

§ 1.163(j)–7 Application of the section 163(j) limitation to foreign corporations and United States shareholders.

(a) *Overview.* This section provides rules for the application of section 163(j) to relevant foreign corporations and United States shareholders of relevant foreign corporations. Paragraph (b) of this section provides the general rule regarding the application of section 163(j) to a relevant foreign corporation. Paragraph (c) of this section provides rules for applying section 163(j) to CFC group members of a CFC group. Paragraph (d) of this section provides rules for determining a specified group and specified group members. Paragraph (e) of this section provides rules and procedures for treating a specified group member as a CFC group member and for determining a CFC group. Paragraph (f) of this section provides rules regarding the treatment of a CFC group member that has ECI. Paragraph (g) of this section provides rules concerning the computation of ATI of an applicable CFC. Paragraph (h) of this section provides a safe-harbor that exempts certain stand-alone applicable CFCs and CFC groups from the application of section 163(j) for a taxable year. Paragraph (i) of this section is reserved. Paragraph (j) of this section provides rules concerning the computation of ATI of a United States shareholder of an applicable CFC. Paragraph (k) of this section provides definitions that apply for purposes of this section. Paragraph (l) of this section provides examples illustrating the application of this section.

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(c) *Application of section 163(j) to CFC group members of a CFC group*—(1) *Scope.* This paragraph (c) provides rules for applying section 163(j) to a CFC group member. Paragraph (c)(2) of this section provides rules for computing a single section 163(j) limitation for a specified period of a CFC group. Paragraph (c)(3) of this section provides rules for allocating a CFC group's section 163(j) limitation to CFC group members for specified taxable years. Paragraph (c)(4) of this section provides currency translation rules. Paragraph (c)(5) of this section provides special rules for specified periods beginning in 2019 or 2020.

(2) *Calculation of section 163(j) limitation for a CFC group for a specified period*—(i) *In general.* A single section 163(j) limitation is computed for a specified period of a CFC group. For purposes of applying section 163(j) and the section 163(j) regulations, the current-year business interest expense, disallowed business interest expense carryforwards, business interest income, floor plan financing interest expense, and ATI of a CFC group for a specified period equal the sums of each CFC group member's respective amounts for its specified taxable year with respect to the specified period. A CFC group member's current-year business interest expense, business interest income, floor plan financing interest expense, and ATI for a specified taxable year are generally determined on a separate-company basis.

(ii) *Certain transactions between CFC group members disregarded.* Any transaction between CFC group members of a CFC group that is entered into with a principal purpose of affecting a CFC group or a CFC group member's section 163(j) limitation by increasing or decreasing a CFC group or a CFC group member's ATI for a specified taxable year is disregarded for purposes of applying section 163(j) and the section 163(j) regulations.

(iii) *CFC group treated as a single C corporation for purposes of allocating items to an excepted trade or business.* For purposes of allocating items to an excepted trade or business under § 1.163(j)–10, all CFC group members of a CFC group are treated as a single C corporation.

(iv) *CFC group treated as a single taxpayer for purposes of determining interest.* For purposes of determining whether amounts, other than amounts in respect of transactions between CFC group members of a CFC group, are treated as interest within the meaning of § 1.163(j)–1(b)(22), all CFC group members of a CFC group are treated as a single taxpayer.

(3) *Deduction of business interest expense*—(i) *CFC group business interest expense*—(A) *In general.* The extent to which a CFC group member's current-year business interest expense and disallowed business interest expense carryforwards for a specified taxable year that ends with or within a specified period may be deducted under section 163(j) is determined under the rules and principles of § 1.163(j)–5(a)(2) and (b)(3)(ii), subject to the modifications described in paragraph (c)(3)(i)(B) of this section.

(B) *Modifications to relevant terms.* For purposes of paragraph (c)(3)(i)(A) of this section, the rules and principles of § 1.163(j)–5(b)(3)(ii) are applied by—

(*1*) Replacing "§ 1.163(j)–4(d)(2)" in § 1.163(j)–5(a)(2)(ii) with "§ 1.163(j)–7(c)(2)(i)";

(*2*) Replacing the term "allocable share of the consolidated group's remaining section 163(j) limitation" with "allocable share of the CFC group's remaining section 163(j) limitation";

(*3*) Replacing the terms "consolidated group" and "group" with "CFC group";

(*4*) Replacing the term "consolidated group's remaining section 163(j) limitation" with "CFC group's remaining section 163(j) limitation";

(*5*) Replacing the term "consolidated return year" with "specified period";

(*6*) Replacing the term "current year" or "current-year" with "current specified period" or "specified taxable year with respect to the current specified period," as the context requires;

(*7*) Replacing the term ''member'' with ''CFC group member''; and

(*8*) Replacing the term ''taxable year'' with ''specified taxable year with respect to a specified period.''

(ii) *Carryforwards treated as attributable to the same taxable year.* For purposes of applying the principles of § 1.163(j)–5(b)(3)(ii), as required under paragraph (c)(3)(i) of this section, CFC group members' disallowed business interest expense carryforwards that arose in specified taxable years with respect to the same specified period are treated as disallowed business interest expense carryforwards from taxable years ending on the same date and are deducted on a pro rata basis, under the principles of § 1.163(j)–5(b)(3)(ii)(C)(*3*), pursuant to paragraph (c)(3)(i) of this section.

(iii) *Multiple specified taxable years of a CFC group member with respect to a specified period.* If a CFC group member has more than one specified taxable year (each year, an *applicable specified taxable year*) with respect to a single specified period of a CFC group, then all such applicable specified taxable years are taken into account for purposes of applying the principles of § 1.163(j)–5(b)(3)(ii), as required under paragraph (c)(3)(i) of this section, with respect to the specified period. The portion of the section 163(j) limitation allocable to disallowed business interest expense carryforwards of the CFC group member for its applicable specified taxable years is prorated among the applicable specified taxable years in proportion to the number of days in each applicable specified taxable year.

(iv) *Limitation on pre-group disallowed business interest expense carryforward*—(A) *General rule*—(*1*) *CFC group member pre-group disallowed business interest expense carryforward.* This paragraph (c)(3)(iv) applies to pre-group disallowed business interest expense carryforwards of a CFC group member. The amount of the pre-group disallowed business interest expense carryforwards described in the preceding sentence that are included in any CFC group member's business interest expense deduction for any specified taxable year under this paragraph (c)(3) may not exceed the aggregate section 163(j) limitation for all specified periods of the CFC group, determined by reference only to the CFC group member's items of income, gain, deduction, and loss, and reduced (including below zero) by the CFC group member's business interest expense (including disallowed business interest expense carryforwards) taken into account as a deduction by the CFC group member in all specified taxable years in which the CFC group member has continuously been a CFC group member of the CFC group (*cumulative section 163(j) pre-group carryforward limitation*).

(*2*) *Subgrouping.* In the case of a CFC group member with a pre-group disallowed business interest expense carryforward (the *loss member*) that joined the CFC group (the *current group*) for a specified taxable year with respect to a specified period (the *relevant period*), if the loss member was a CFC group member of a different CFC group (the *former group*) immediately prior to joining the current group, a pre-group subgroup is composed of the loss member and each other CFC group member that became a CFC group member of the current group for a specified taxable year with respect to the relevant period and was a member of the former group immediately prior to joining the current group. For purposes of this paragraph (c), the rules and principles of § 1.163(j)–5(d)(1)(B) apply to a pre-group subgroup as if the pre-group subgroup were a SRLY subgroup.

(B) *Deduction of pre-group disallowed business interest expense carryforwards.* Notwithstanding paragraph (c)(3)(iv)(A)(*1*) of this section, pre-group disallowed business interest expense carryforwards are available for deduction by a CFC group member in its specified taxable year only to the extent the CFC group has remaining section 163(j) limitation for the specified period after the deduction of current-year business interest expense and disallowed business interest expense carryforwards from earlier taxable years that are permitted to be deducted in specified taxable years of CFC group members with respect to the specified period. See paragraph (c)(3)(i) of this section and § 1.163(j)–5(b)(3)(ii)(A). Pre-group disallowed business interest expense carryforwards are deducted on a pro rata basis (under the principles of paragraph (c)(3)(i) of this section and § 1.163(j)–5(b)(3)(ii)(C)(*3*)) with other disallowed business interest expense carryforwards from taxable years ending on the same date.

(4) *Currency translation.* For purposes of applying this paragraph (c), items of a CFC group member are translated into a single currency for the CFC group and back to the functional currency of the CFC group member using the average rate for the CFC group member's specified taxable year, using any reasonable method, consistently applied. The single currency for the CFC group may be the U.S. dollar or the functional currency of a plurality of the CFC group members.

(5) *Special rule for specified periods beginning in 2019 or 2020*—(i) *50 percent ATI limitation applies to a specified period of a CFC group.* In the case of a CFC group, § 1.163(j)–2(b)(2) (including the election under § 1.163(j)–2(b)(2)(ii)) applies to a specified period of the CFC group beginning in 2019 or 2020, rather than to a specified taxable year of a CFC group member. An election under § 1.163(j)–2(b)(2)(ii) for a specified period of a CFC group is not effective unless made by each designated U.S. person. Except as otherwise provided in this paragraph (c)(5)(i), the election is made in accordance with Revenue Procedure 2020–22, 2020–18 I.R.B. 745. For purposes of applying § 1.964–1(c), the election is treated as if made for each CFC group member.

(ii) *Election to use 2019 ATI applies to a specified period of a CFC group*—(A) *In general.* In the case of a CFC group, for purposes of applying paragraph (c)(2) of this section, an election under § 1.163(j)–2(b)(3)(i) is made for a specified period of a CFC group beginning in 2020 and applies to the specified taxable years of each CFC group member with respect to such specified period, taking into account the application of paragraph (c)(5)(ii)(B) of this section. The election under § 1.163(j)–2(b)(3)(i) does not apply to any specified taxable year of a CFC group member other than those described in the preceding sentence. An election under § 1.163(j)–2(b)(3)(i) for a specified period of a CFC group is not effective unless made by each designated U.S. person. Except as otherwise provided in this paragraph (c)(5)(ii)(A), the election is made in accordance with Revenue Procedure 2020–22, 2020–18 I.R.B. 745. For purposes of applying § 1.964–1(c), the election is treated as if made for each CFC group member.

(B) *Specified taxable years that do not begin in 2020.* If a specified taxable year of a CFC group member with respect to the specified period described in paragraph (c)(5)(ii)(A) of this section begins in 2019, then, for purposes of applying paragraph (c)(2) of this section, § 1.163(j)–2(b)(3) is applied to such specified taxable year by substituting ''2018'' for ''2019'' and ''2019'' for ''2020.'' If a specified taxable year of a CFC group member with respect to the specified period described in paragraph (c)(5)(ii)(A) of this section begins in 2021, then, for purposes of applying paragraph (c)(2) of this section, § 1.163(j)–2(b)(3) is applied to such specified taxable year by substituting ''2020'' for ''2019'' and ''2021'' for ''2020.''

(d) *Determination of a specified group and specified group members*—(1) *Scope.* This paragraph (d) provides rules for determining a specified group and specified group members. Paragraph (d)(2) of this section provides rules for determining a specified group. Paragraph (d)(3) of this section provides rules for determining specified group members.

(2) *Rules for determining a specified group*—(i) *Definition of a specified group.* Subject to paragraph (d)(2)(ii) of this section, the term *specified group* means one or more chains of applicable CFCs connected through stock ownership with a specified group parent (which is included in the specified group only if it is an applicable CFC), but only if—

(A) The specified group parent owns directly or indirectly stock meeting the requirements of section 1504(a)(2)(B) in at least one applicable CFC; and

(B) Stock meeting the requirements of section 1504(a)(2)(B) in each of the applicable CFCs (except the specified group parent) is owned directly or indirectly by one or more of the other applicable CFCs or the specified group parent.

(ii) *Indirect ownership.* For purposes of applying paragraph (d)(2)(i) of this section, stock is owned indirectly only if it is owned under section 318(a)(2)(A) through a partnership or under section 318(a)(2)(A) or (B) through an estate or trust not described in section 7701(a)(30).

(iii) *Specified group parent.* The term *specified group parent* means a qualified U.S. person or an applicable CFC.

(iv) *Qualified U.S. person.* The term *qualified U.S. person* means a United States person described in section 7701(a)(30)(A) or (C). For purposes of this paragraph (d), members of a consolidated group that file (or that are required to file) a consolidated U.S. federal income tax return are treated as a single qualified U.S person and individuals described in section 7701(a)(30)(A) whose filing status is married filing jointly are treated as a single qualified U.S. person.

(v) *Stock.* For purposes of paragraph (d)(3)(i) of this section, the term *stock* has the same meaning as ''stock'' in section 1504 (without regard to § 1.1504–4, except as provided in paragraph (d)(2)(vi) of this section) and all shares of stock within a single class are considered to have the same value. Thus, control premiums and minority and blockage discounts within a single class are not taken into account.

(vi) *Options treated as exercised.* For purposes of this paragraph (d)(2), options that are reasonably certain to be exercised, as determined under § 1.1504–4(g), are treated as exercised. For purposes of this paragraph (d)(2)(vi), options include call options, warrants, convertible obligations, put options, and any other instrument treated as an option under § 1.1504–4(d), determined by replacing the term ''a principal purpose of avoiding the application of section 1504 and this section'' with ''a principal purpose of avoiding the application of section 163(j).''

(vii) *When a specified group ceases to exist.* The principles of § 1.1502–75(d)(1), (d)(2)(i) through (d)(2)(ii), and (d)(3)(i) through (d)(3)(iv), apply for purposes of determining when a specified group ceases to exist. Solely for purposes of applying these principles, each applicable CFC that is treated as a specified group member for a taxable year with respect to a specified period is treated as affiliated with the specified group parent from the beginning to the end of the specified period, without regard to the beginning or end of its taxable year.

(3) *Rules for determining a specified group member.* If an applicable CFC is included in a specified group on the last day of a taxable year of the applicable CFC that ends with or within a specified period, the applicable CFC is a *specified group member* with respect to the specified period for its entire taxable year ending with or within the specified period. If an applicable CFC has multiple taxable years that end with or within a specified period, this paragraph (d)(3) is applied separately to each taxable year to determine if the applicable CFC is a specified group member for such taxable year.

(e) *Rules and procedures for treating a specified group as a CFC group*—(1) *Scope.* This paragraph (e) provides rules and procedures for treating a specified group member as a CFC group member and for determining a CFC group for purposes of applying section 163(j) and the section 163(j) regulations.

(2) *CFC group and CFC group member*—(i) *CFC group.* The term *CFC group* means, with respect to a specified period, all CFC group members for their specified taxable years.

(ii) *CFC group member.* The term *CFC group member* means, with respect to a specified taxable year and a specified period, a specified group member of a specified group for which a CFC group election is in effect.

(3) *Duration of a CFC group.* A CFC group continues until the CFC group election is revoked, or there is no longer a specified period with respect to the specified group.

(4) *Joining or leaving a CFC group.* If an applicable CFC becomes a specified group member for a specified taxable year with respect to a specified period of a specified group for which a CFC group election is in effect, the CFC group election applies to the applicable CFC and the applicable CFC becomes a CFC group member. If an applicable CFC ceases to be a specified group member for a specified taxable year with respect to a specified period of a specified group for which a CFC group election is in effect, the CFC group election terminates solely with respect to the applicable CFC.

(5) *Manner of making or revoking a CFC group election*—(i) *In general.* An election is made or revoked under this paragraph (e)(5) (a *CFC group election*) with respect to a specified period of a specified group. A CFC group election remains in effect for each specified period of the specified group until revoked. A CFC group election that is in effect with respect to a specified period of a specified group applies to each specified group member for its specified taxable year that ends with or within the specified period. The making or revoking of a CFC group election is not effective unless made or revoked by each designated U.S. person.

(ii) *Revocation by election.* A CFC group election cannot be revoked with respect to any specified period beginning prior to 60 months following the last day of the specified period for which the election was made. Once a CFC group election has been revoked, a new CFC group election cannot be made with respect to any specified period beginning prior to 60 months following the last day of the specified period for which the election was revoked.

(iii) *Timing.* A CFC group election must be made or revoked with respect to a specified period of a specified group no later than the due date (taking into account extensions, if any) of the original Federal income tax return for the taxable year of each designated U.S. person in which or with which the specified period ends.

(iv) *Election statement.* Except as otherwise provided in publications, forms, instructions, or other guidance, to make or revoke a CFC group election for a specified period of a specified group, each designated U.S. person must attach a statement to its relevant Federal tax or information return. The statement must include the name and taxpayer identification number of all designated U.S. persons, a statement that the CFC group election is being made or revoked, as applicable, the specified period for which the CFC group election is being made or revoked, and the name of each CFC group member and its specified taxable year with respect to the specified period. The statement must be filed in the manner prescribed in publications, forms, instructions, or other guidance.

(v) *Effect of prior CFC group election.* A CFC group election is made solely pursuant to the provisions of this paragraph (e)(5), without regard to whether the election described in proposed § 1.163(j)–7(f)(7) that was included in a notice of proposed rulemaking (REG–106089–18) that was published on December 28, 2018, in the **Federal Register** (83 FR 67490) was in effect.

(f) *Treatment of a CFC group member that has ECI*—(1) *In general.* If a CFC group member has ECI in its specified taxable year, then for purposes of section 163(j) and the section 163(j) regulations—

(i) The items, disallowed business interest expense carryforwards, and other attributes of the CFC group member that are ECI are treated as items, disallowed business interest expense carryforwards, and attributes of a separate applicable CFC (such deemed corporation, an *ECI deemed corporation*), subject to § 1.163(j)–8(d), that has same taxable year and shareholders as the applicable CFC; and

(ii) The ECI deemed corporation is not treated as a specified group member for the specified taxable year.

(2) *Ordering rule.* Paragraph (f)(1) of this section applies before application of § 1.163(j)–8(d).

(g) * * *

(3) *Treatment of certain taxes.* For purposes of computing the ATI of a relevant foreign corporation for a taxable year, tentative taxable income takes into account any deduction for foreign taxes. See section 164(a).

(4) *Anti-abuse rule*—(i) *In general.* If a specified group member of a specified group or an applicable partnership (*specified lender*) includes an amount (the *payment amount*) in income and such amount is attributable to business interest expense incurred by another specified group member or an applicable partnership of the specified group (a *specified borrower*) during its taxable year, then the ATI of the specified borrower for the taxable year is increased by the ATI adjustment amount if—

(A) The business interest expense is incurred with a principal purpose of reducing the Federal income tax liability of any United States shareholder of a specified group member (including over multiple taxable years);

(B) Absent the application of this paragraph (g)(4), the effect of the specified borrower treating all or part of the payment amount as disallowed business interest expense would be to reduce the Federal income tax liability of any United States shareholder of a specified group member; and

(C) Either no CFC group election is in effect with respect to the specified group or the specified borrower is an applicable partnership.

(ii) *ATI adjustment amount*—(A) *In general.* For purposes of this paragraph (g)(4), the term *ATI adjustment amount* means, with respect to a specified borrower and a taxable year, the product of 3⅓ and the lesser of the payment amount or the disallowed business interest expense, computed without regard to this paragraph (g)(4).

(B) *Special rule for taxable years or specified periods beginning in 2019 or 2020.* For any taxable year of an applicable CFC or specified taxable year of a CFC group member with respect to a specified period for which the section 163(j) limitation is determined based, in part, on 50 percent of ATI, in accordance with § 1.163(j)–2(b)(2), paragraph (g)(4)(ii)(A) of this section is applied by substituting ''2'' for ''3⅓.''

(iii) *Applicable partnership.* For purposes of this paragraph (g)(4), the term *applicable partnership* means, with respect to a specified group, a partnership in which at least 80 percent of the interests in capital or profits is owned, directly or indirectly through one or more other partnerships, by specified group members of the specified group.

(h) *Election to apply safe-harbor*—(1) *In general.* If an election to apply this paragraph (h)(1) (*safe-harbor election*) is in effect with respect to a taxable year of a stand-alone applicable CFC or a specified taxable year of a CFC group member, as applicable, then, for such year, no portion of the applicable CFC's business interest expense is disallowed under the section 163(j) limitation. This paragraph (h) does not apply to excess business interest expense, as described in § 1.163(j)–6(f)(2), until the taxable year in which it is treated as paid or accrued by an applicable CFC under § 1.163(j)–6(g)(2)(i). Furthermore, excess business interest expense is not taken into account for purposes of determining whether the safe-harbor election is available for a stand-alone applicable CFC or a CFC group until the taxable year in which it is treated as paid or accrued by an applicable CFC under § 1.163(j)–6(g)(2)(i).

(2) *Eligibility for safe-harbor election*—(i) *Stand-alone applicable CFC.* The safe-harbor election may be made for the taxable year of a stand-alone applicable CFC only if business interest expense of the applicable CFC is less than or equal to 30 percent of the lesser of qualified tentative taxable income or the eligible amount of the applicable CFC for its taxable year.

(ii) *CFC group*—(A) *In general.* The safe-harbor election may be made for the specified period of a CFC group only if the business interest expense of the CFC group for the specified period is less than or equal to 30 percent of the lesser of the sum of qualified tentative taxable income or the sum of the eligible amounts of each CFC group member for its specified taxable year with respect to the specified period, and no CFC group member has pre-group disallowed business interest expense carryforward.

(B) *Currency translation.* For purposes of applying paragraph (h)(2)(ii) of this section, qualified tentative taxable income and eligible amounts of each CFC group member are translated into the currency in which the business interest expense of the CFC group is denominated using the method used under paragraph (c)(4) of this section. See paragraph (c)(2)(i) of this section for rules for determining the business interest expense of a CFC group.

(3) *Eligible amount*—(i) *In general.* Subject to paragraph (h)(3)(ii) of this section, the term *eligible amount* means, with respect to the taxable year of an applicable CFC, the sum of the following amounts, computed without regard to the application of section 163(j) and the section 163(j) regulations (including without regard to any disallowed business interest expense carryforwards)—

(A) Subpart F income (within the meaning of section 952);

(B) The product of—

(*1*) The excess of 100 percent over the percentage described in section 250(a)(1)(B), taking into account section 250(a)(3)(B), and

(*2*) The excess, if any, of tested income (within the meaning of section 951A(c)(2)(A) and § 1.951A–2(b)(1)), over the CFC-level net deemed tangible income return.

(ii) *Amounts properly allocable to a non-excepted trade or business.* For purposes of computing an eligible amount, subpart F income and tested income are determined by only taking into account items properly allocable to a non-excepted trade or business.

(4) *Qualified tentative taxable income.* The term *qualified tentative taxable income* means, with respect to a taxable year of an applicable CFC, the applicable CFC's tentative taxable income, determined by only taking into

account items properly allocable to a non-excepted trade or business.

(5) *Manner of making a safe-harbor election*—(i) *In general.* A safe-harbor election is an annual election made under this paragraph (h)(5) with respect to a taxable year of a stand-alone applicable CFC or with respect to a specified period of a CFC group. A safe-harbor election that is made with respect to a specified period of a CFC group is effective with respect to each CFC group member for its specified taxable year. A safe-harbor election is only effective if made by each designated U.S. person with respect to a stand-alone applicable CFC or a CFC group. A safe-harbor election is made with respect to a taxable year of a stand-alone applicable CFC, or a specified period of a CFC group, no later than the due date (taking into account extensions, if any) of the original Federal income tax return for the taxable year of each designated U.S. person, respectively, in which or with which the taxable year of the stand-alone applicable CFC ends or the specified period of the CFC group ends.

(ii) *Election statement.* Unless otherwise provided in publications, forms, instructions, or other guidance, to make a safe-harbor election, each designated U.S. person must attach to its relevant Federal income tax return or information return a statement that includes the name and taxpayer identification number of all designated U.S. persons, a statement that a safe-harbor election is being made pursuant to § 1.163(j)–7(h) and that the requirements for making the election are satisfied, and the taxable year of the stand-alone applicable CFC or the specified period of the CFC group, as applicable, for which the safe-harbor election is being made. In the case of a CFC group, the statement must also include the name of each CFC group member and its specified taxable year that ends with or within the specified period for which the safe-harbor election is being made. The statement must be filed in the manner prescribed in publications, forms, instructions, or other guidance.

(6) *Special rule for taxable years or specified periods beginning in 2019 or 2020.* In the case of a stand-alone applicable CFC, for any taxable year beginning in 2019 or 2020, paragraph (h)(2)(i) of this section is applied by substituting ''50 percent'' for ''30 percent.'' In the case of a CFC group, for any specified period beginning in 2019 or 2020, paragraph (h)(2)(ii)(A) of this section is applied by substituting ''50 percent'' for ''30 percent.''

* * * * *

(j) *Rules regarding the computation of ATI of certain United States shareholders of applicable CFCs*—(1) *In general.* For purposes of computing ATI of a United States shareholder of an applicable CFC, for the taxable year of the United States shareholder in which or with which the taxable year of the applicable CFC ends, there is added to the United States shareholder's tentative taxable income the product of—

(i) The portion of the adjustment, if any, made to the United States shareholder's tentative taxable income under § 1.163(j)–1(b)(1)(ii)(G) (regarding specified deemed inclusions) that is attributable to the applicable CFC, but for this purpose excluding the portion of the adjustment that is attributable to an inclusion under section 78 with respect to the applicable CFC; and

(ii) A fraction, expressed as a percentage, but not greater than 100 percent, the numerator of which is CFC excess taxable income and the denominator of which is the ATI of the applicable CFC for the taxable year.

(2) *Rules for determining CFC excess taxable income*—(i) *In general.* The term *CFC excess taxable income* means, with respect to a taxable year of an applicable CFC, the amount described in paragraph (j)(2)(ii) or (j)(2)(iii) of this section, as applicable.

(ii) *Applicable CFC is a stand-alone applicable CFC.* If an applicable CFC is a stand-alone applicable CFC for a taxable year, its CFC excess taxable income for the taxable year is the amount that bears the same ratio to the applicable CFC's ATI as—

(A) The excess (if any) of—

(*1*) 30 percent of the applicable CFC's ATI; over

(*2*) The amount (if any) by which the applicable CFC's business interest expense exceeds its business interest income and floor plan financing interest expense; bears to

(B) 30 percent of the applicable CFC's ATI.

(iii) *Applicable CFC is a CFC group member.* If an applicable CFC is a CFC group member for a specified taxable year, its CFC excess taxable income is equal to the product of the CFC group member's ATI percentage and the amount that bears the same ratio to the CFC group's ATI for the specified period as—

(A) The excess (if any) of—

(*1*) 30 percent of the CFC group's ATI; over

(*2*) The amount (if any) by which the CFC group's business interest expense exceeds the CFC group's business interest income and floor plan financing interest expense; bears to

(B) 30 percent of the CFC group's ATI.

(iv) *ATI percentage.* For purposes of this paragraph (j), the term *ATI percentage* means, with respect to a specified taxable year of a CFC group member and a specified period of the CFC group, a fraction (expressed as a percentage), the numerator of which is the ATI of the CFC group member for the specified taxable year, and the denominator of which is the ATI of the CFC group for the specified period. If either the numerator or denominator of the fraction is less than or equal to zero, the ATI percentage is zero.

(3) *Cases in which an addition to tentative taxable income is not allowed.* Paragraph (j)(1) of this section is not applicable for a taxable year of a United States shareholder if, with respect to the taxable year of the applicable CFC described in paragraph (j)(1) of this section—

(i) A safe-harbor election (as described in paragraph (h) of this section) is in effect; or

(ii) The applicable CFC is neither a stand-alone applicable CFC nor a CFC group member.

(4) *Special rule for taxable years or specified periods beginning in 2019 or 2020.* In the case of a stand-alone applicable CFC, for any taxable year beginning in 2019 or 2020 to which the election described in § 1.163(j)–2(b)(2)(ii) does not apply, paragraph (j)(2)(ii) of this section is applied by substituting ''50 percent'' for ''30 percent'' each place it appears. In the case of a CFC group member, for any specified taxable year with respect to a specified period beginning in 2019 or 2020 to which the election described in § 1.163(j)–2(b)(2)(ii) does not apply, paragraph (j)(2)(iii) of this section is applied by substituting ''50 percent'' for ''30 percent'' each place it appears.

(k) *Definitions.* The following definitions apply for purposes of this section.

(1) *Applicable partnership.* The term *applicable partnership* has the meaning provided in paragraph (g)(4)(iii) of this section.

(2) *Applicable specified taxable year.* The term *applicable specified taxable year* has the meaning provided in paragraph (c)(3)(iii) of this section.

(3) *ATI adjustment amount.* The term *ATI adjustment amount* has the meaning provided in paragraph (g)(4)(ii) of this section.

(4) *ATI percentage.* The term *ATI percentage* has the meaning provided in paragraph (j)(2)(iv) of this section.

(5) *CFC excess taxable income.* The term *CFC excess taxable income* has the meaning provided in paragraph (j)(2)(i) of this section.

(6) *CFC group.* The term *CFC group* has the meaning provided in paragraph (e)(2)(i) of this section.

(7) *CFC group election.* The term *CFC group election* means the election described in paragraph (e)(5) of this section.

(8) *CFC group member.* The term *CFC group member* has the meaning provided in paragraph (e)(2)(ii) of this section.

(9) *CFC-level net deemed tangible income return*—(i) *In general.* The term *CFC-level net deemed tangible income return* means, with respect to a taxable year of an applicable CFC, the excess (if any) of—

(A) 10 percent of the qualified business asset investment, as defined in section 951A(d)(1) and § 1.951A–3(b), of the applicable CFC, over

(B) The excess, if any, of—

(*1*) Tested interest expense, as defined in § 1.951A–4(b)(1), of the applicable CFC, over

(*2*) Tested interest income, as defined in § 1.951A–4(b)(2), of the applicable CFC.

(ii) *Amounts properly allocable to a non-excepted trade or business.* For purposes of computing CFC-level net deemed tangible income return, qualified business asset investment is determined by only taking into account assets properly allocable to a non-excepted trade or business, as determined in § 1.163(j)–10(c)(3), and tested interest expense and tested interest income are determined by only taking into account items properly allocable to a non-excepted trade or business, as determined in § 1.163(j)–10(c).

(10) *Cumulative section 163(j) pre-group carryforward limitation.* The term *cumulative section 163(j) pre-group carryforward limitation* has the meaning provided in paragraph (c)(3)(iv)(A)(*1*) of this section.

(11) *Current group.* The term *current group* has the meaning provided in paragraph (c)(3)(iv)(A)(*2*) of this section.

(12) *Designated U.S. person.* The term *designated U.S. person* means—

(i) With respect to a stand-alone applicable CFC, each controlling domestic shareholder, as defined in § 1.964–1(c)(5) of the applicable CFC; or

(ii) With respect to a specified group, the specified group parent, if the specified group parent is a qualified U.S. person, or each controlling domestic shareholder, as defined in § 1.964–1(c)(5), of the specified group parent, if the specified group parent is an applicable CFC.

(13) *ECI deemed corporation.* The term *ECI deemed corporation* has the meaning provided in paragraph (f)(1)(i) of this section.

(14) *Effectively connected income.* The term *effectively connected income* (or *ECI*) means income or gain that is ECI, as defined in § 1.884–1(d)(1)(iii), and deduction or loss that is allocable to, ECI, as defined in § 1.884–1(d)(1)(iii).

(15) *Eligible amount.* The term *eligible amount* has the meaning provided in paragraph (h)(3)(i) of this section.

(16) *Former group.* The term *former group* has the meaning provided in paragraph (c)(3)(iv)(A)(*2*) of this section.

(17) *Loss member.* The term *loss member* has the meaning provided in paragraph (c)(3)(iv)(A)(*2*) of this section.

(18) *Payment amount.* The term *payment amount* has the meaning provided in paragraph (g)(4)(i) of this section.

(19) *Pre-group disallowed business interest expense carryforward.* The term *pre-group disallowed business interest expense carryforward* means, with respect to a CFC group member and a specified taxable year, any disallowed business interest expense carryforward of the CFC group member that arose in a taxable year during which the CFC group member (or its predecessor) was not a CFC group member of the CFC group.

(20) *Qualified tentative taxable income.* The term *qualified tentative taxable income* has the meaning provided in paragraph (h)(4) of this section.

(21) *Qualified U.S. person.* The term *qualified U.S. person* has the meaning provided in paragraph (d)(2)(iv) of this section.

(22) *Relevant period.* The term *relevant period* has the meaning provided in paragraph (c)(3)(iv)(A)(*2*) of this section.

(23) *Safe-harbor election.* The term *safe-harbor election* has the meaning provided in paragraph (h)(1) of this section.

(24) *Specified borrower.* The term *specified borrower* has the meaning provided in paragraph (g)(4)(i) of this section.

(25) *Specified group.* The term *specified group* has the meaning provided in paragraph (d)(2)(i) of this section.

(26) *Specified group member.* The term *specified group member* has the meaning provided in paragraph (d)(3) of this section.

(27) *Specified group parent.* The term *specified group parent* has the meaning provided in paragraph (d)(2)(iii) of this section.

(28) *Specified lender.* The term *specified lender* has the meaning provided in paragraph (g)(4)(i) of this section

(29) *Specified period*—(i) *In general.* Except as otherwise provided in paragraph (k)(29)(ii) of this section, the term *specified period* means, with respect to a specified group—

(A) If the specified group parent is a qualified U.S. person, the period ending on the last day of the taxable year of the specified group parent and beginning on the first day after the last day of the specified group's immediately preceding specified period; or

(B) If the specified group parent is an applicable CFC, the period ending on the last day of the specified group parent's required year described in section 898(c)(1), without regard to section 898(c)(2), and beginning on the first day after the last day of the specified group's immediately preceding specified period.

(ii) *Short specified period.* A specified period begins no earlier than the first date on which a specified group exists. A specified period ends on the date a specified group ceases to exist under paragraph (d)(2)(vii) of this section. If the last day of a specified period, as determined under paragraph (k)(29)(i) of this section, changes, and, but for this paragraph (k)(29)(ii), the change in the last day of the specified period would result in the specified period being longer than 12 months, the specified period ends on the date on which the specified period would have ended had the change not occurred.

(30) *Specified taxable year.* The term *specified taxable year* means, with respect to an applicable CFC that is a specified group member of a specified group and a specified period, a taxable year of the applicable CFC that ends with or within the specified period.

(31) *Stand-alone applicable CFC.* The term *stand-alone applicable CFC* means any applicable CFC that is not a specified group member.

(32) *Stock.* The term *stock* has the meaning provided in paragraph (d)(2)(v) of this section.

(l) *Examples.* The following examples illustrate the application of this section. For each example, unless otherwise stated, no exemptions from the application of section 163(j) are available, no foreign corporation has ECI, and all relevant taxable years and specified periods begin after December 31, 2020.

(1) *Example 1. Specified taxable years included in specified period of a specified*

group—(i) *Facts.* As of June 30, Year 1, USP, a domestic corporation, owns 60 percent of the common stock of FP, which owns all of the stock of FC1, FC2, and FC3. The remaining 40 percent of the common stock of FP is owned by an unrelated foreign corporation. FP has a single class of stock. FP acquired the stock of FC3 from an unrelated person on March 22, Year 1. The acquisition did not result in a change in FC3's taxable year or a close of its taxable year. USP's interest in FP and FP's interest in FC1 and FC2 has been the same for a number of years. USP has a taxable year ending June 30, Year 1, which is not a short taxable year. Each of FP, FC1, FC2, and FC3 are applicable CFCs. Pursuant to section 898(c)(2), FP and FC1 have taxable years ending May 31, Year 1. Pursuant to section 898(c)(1), FC2 and FC3 have taxable years ending June 30, Year 1.

(ii) *Analysis*—(A) *Determining a specified group and specified period of the specified group.* Pursuant to paragraph (d) of this section, FP, FC1, FC2, and FC3 are members of a specified group, and FP is the specified group parent. Because the specified group parent, FP, is an applicable CFC, the specified period of the specified group is the period ending on June 30, Year 1, which is the last day of FP's required year described in section 898(c)(1), without regard to section 898(c)(2), and on beginning July 1, Year 0, which is the first day following the last day of the specified group's immediately preceding specified period (June 30, Year 0). See paragraph (k)(29)(i)(B) of this section.

(B) *Determining the specified taxable years with respect to the specified period.* Pursuant to paragraph (d)(3) of this section, because each of FP and FC1 are included in the specified group on the last day of their taxable years ending May 31, Year 1 and such taxable years end with or within the specified period ending June 30, Year 1, FP and FC1 are specified group members with respect to the specified period ending June 30, Year 1, for their entire taxable years ending May 31, Year 1, and those taxable years are specified taxable years. Similarly, because each of FC2 and FC3 are included in the specified group on the last day of their taxable years ending June 30, Year 1, and such taxable years end with or within the specified period ending June 30, Year 1, FC2 and FC3 are specified group members with respect to the specified period ending June 30, Year 1, for their entire taxable years ending June 30, Year 1, and those taxable years are specified taxable years. The fact that FC3 was acquired on March 22, Year 1, does not prevent FC3 from being a specified group member with respect to the specified period for the portion of its specified taxable year prior to March 22, Year 1.

(2) *Example 2. CFC groups*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (l)(1)(i) of this section. In addition, a CFC group election is in place with respect to the specified period ending June 30, Year 1.

(ii) *Analysis.* Because a CFC group election is in place for the specified period ending June 30, Year 1, pursuant to paragraph (e)(2)(ii) of this section, each specified group member is a CFC group member with respect to its specified taxable year ending with or within the specified period. Accordingly, FP, FC1, FC2, and FC3 are CFC group members with respect to the specified period ending June 30, Year 1, for their specified taxable years ending May 31, Year 1, and June 30, Year 1, respectively. Pursuant to paragraph (e)(2)(i) of this section, the CFC group for the specified period ending June 30, Year 1, consists of FP, FC1, FC2, and FC3 for their specified taxable years ending May 31, Year 1, and June 30, Year 1, respectively. Pursuant to paragraph (c)(2) of this section, a single section 163(j) limitation is computed for the specified period ending June 30, Year 1. That section 163(j) calculation will include FP and FC1's specified taxable years ending May 31, Year 1, and FC2 and FC3's specified taxable years ending June 30, Year 1.

(3) *Example 3. Application of anti-abuse rule*—(i) *Facts.* USP, a domestic corporation, is the specified group parent of a specified group. The specified group members include CFC1 and CFC2. USP owns (within the meaning of section 958(a)) all of the stock of all specified group members. USP has a calendar year taxable year. All specified group members also have a calendar year taxable year and a functional currency of the U.S. dollar. CFC1 is organized in, and a tax resident of, a jurisdiction that imposes no tax on certain types of income, including interest income. With respect to Year 1, USP expects to pay no residual U.S. tax on its income inclusion under section 951A(a) (GILTI inclusion) and expects to have unused foreign tax credits in the category described in section 904(d)(1)(A). A CFC group election is not in effect for Year 1. With a principal purpose of reducing USP's Federal income tax liability, on January 1, Year 1, CFC1 loans $100x to CFC2. On December 31, Year 1, CFC2 pays interest of $10x to CFC1 and repays the principal of $100x. Absent application of paragraph (g)(4)(i) of this section, CFC2 would treat all $10x of interest expense as disallowed business interest expense and therefore would have $10x of disallowed business interest expense carryforward to Year 2. In Year 2, CFC2 disposes of one of its businesses at a substantial gain that gives rise to tested income (within the meaning of section 951A(c)(2)(A) and § 1.951A–2(b)(1)). Assume that as a result of the gain being included in the ATI of CFC2, absent application of paragraph (g)(3)(i) of this section, CFC2 would be allowed to deduct the entire $10x of disallowed business interest expense carryforward and therefore reduce the amount of CFC2's tested income. Also, assume that USP would have residual U.S. tax on its GILTI inclusion in Year 2, without regard to the application of paragraph (g)(4)(i) of this section.

(ii) *Analysis.* The $10x of interest expense paid in Year 1 is a payment amount described in paragraph (g)(4)(i) of this section because it is between specified group members, CFC1 and CFC2. Furthermore the requirements of paragraph (g)(4)(i)(A), (B), and (C) of this section are satisfied because the business interest expense is incurred with a principal purpose of reducing USP's Federal income tax liability; absent the application of paragraph (g)(4)(i) of this section, the effect of CFC2 treating the $10x of business interest expense as disallowed business interest expense in Year 1 would be to reduce USP's Federal income tax liability in Year 2; and no CFC group election is in effect with respect to the specified group in Year 1. Because the requirements of paragraph (g)(4)(i)(A), (B), and (C) of this section are satisfied, CFC2's ATI for Year 1 is increased by $33.33x, which is the amount equal to 3 ⅓ multiplied by $10x (the lesser of the payment amount of $10x and the disallowed business interest expense of $10x). As a result, the $10x of business interest expense is not treated by CFC2 as disallowed business interest expense in Year 1, and therefore does not give rise to a disallowed business interest expense carryforward to Year 2.

(m) *Applicability dates*—(1) *General applicability date.* Except as provided in paragraph (m)(2) of this section, this section applies to taxable years of a foreign corporation beginning on or after November 13, 2020 However, except as provided in paragraph (m)(2) of this section, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of this section to a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties consistently apply the rules of this section to each subsequent taxable year and the section 163(j) regulations, and if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.382–7, 1.383–0, 1.383–1, 1.469–9, 1.469–11, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–36, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4 to that taxable year and each subsequent taxable year.

(2) *Exception.* Paragraphs (a), (c) through (f), (g)(3) and (4), and (h) through (k) of this section apply to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply paragraphs (a), (c) through (f), (g)(3) and (4), and (h) through (k) of this section in their entirety for a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties also apply § 1.163(j)–8 for the taxable year. For taxable years beginning before November 13, 2020, taxpayers and their related parties may not choose to apply paragraphs (a), (c) through (f), (g)(3) and (4), and (h) through (k) of this section unless they also apply paragraphs (b) and (g)(1) and (2) of this section in accordance with

the second sentence of paragraph (m)(1) of this section. Notwithstanding paragraph (e)(5)(iii) or (h)(5)(i) of this section, in the case of a specified period of a specified group or a taxable year of a stand-alone applicable CFC that ends with or within a taxable year of a designated U.S. person ending before November 13, 2020, a CFC group election or a safe-harbor election may be made on an amended Federal income tax return filed on or before the due date (taking into account extensions, if any) of the original Federal income tax return for the first taxable year of each designated U.S. person ending after November 13, 2020.

■ **Par. 9.** As reserved in a final rule elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.163(j)–8 is added to read as follows:

§ 1.163(j)–8 Application of the section 163(j) limitation to foreign persons with effectively connected income.

(a) *Overview.* This section provides rules concerning the application of section 163(j) to foreign persons with ECI. Paragraph (b) of this section modifies the application of section 163(j) for a specified foreign person with ECI. Paragraph (c) of this section sets forth rules for a specified foreign partner in a partnership with ECI. Paragraph (d) of this section allocates disallowed business interest expense for relevant foreign corporations with ECI. Paragraph (e) of this section provides rules concerning disallowed business interest expense. Paragraph (f) of this section coordinates the application of section 163(j) with § 1.882–5 and the branch profits tax under section 884. Paragraph (g) of this section provides definitions that apply for purposes of this section. Paragraph (h) of this section illustrates the application of this section through examples.

(b) *Application to a specified foreign person with ECI*—(1) *In general.* If a taxpayer is a specified foreign person, then the taxpayer applies the modifications described in this paragraph (b), taking into account the application of paragraph (c) of this section.

(2) *Modification of adjusted taxable income.* Adjusted taxable income for a specified foreign person for a taxable year means the specified foreign person's adjusted taxable income, as determined under § 1.163(j)–1(b)(1), taking into account only items that are ECI.

(3) *Modification of business interest expense.* Business interest expense for a specified foreign person means business interest expense described in § 1.163(j)–1(b)(3) that is ECI, taking into account the application of paragraph (f)(1)(iii) of this section.

(4) *Modification of business interest income.* The business interest income of a specified foreign person means business interest income described in § 1.163(j)–1(b)(4) that is ECI.

(5) *Modification of floor plan financing interest expense.* The floor plan financing interest expense of a specified foreign person means floor plan financing interest expense described § 1.163(j)–1(b)(19) that is ECI.

(6) *Modification of allocation of interest expense and interest income that is allocable to a trade or business.* For purposes of applying § 1.163(j)–10(c) to a specified foreign person, only interest income and interest expense that are ECI and only assets that are U.S. assets, as defined in § 1.884–1(d), are taken into account. If the specified foreign person is also a specified foreign partner, this paragraph (b)(6) does not apply to any trade or business of the partnership.

(c) *Rules for a specified foreign partner*—(1) *Characterization of excess taxable income*—(i) *In general.* The portion of excess taxable income allocated to a specified foreign partner from a partnership pursuant to § 1.163(j)–6(f)(2) that is ECI is equal to the specified foreign partner's allocation of excess taxable income from the partnership multiplied by its specified ATI ratio with respect to the partnership, and the remainder is not ECI.

(ii) *Specified ATI ratio.* The term *specified ATI ratio* means the fraction described in this paragraph (c)(1)(ii). If the specified foreign partner's distributive share of ECI and distributive share of non-ECI are both positive, the numerator of this fraction is the specified foreign partner's distributive share of ECI and the denominator is the specified foreign partner's distributive share of partnership items of income, gain, deduction, and loss. If the specified foreign partner's distributive share of ECI is negative or zero and its distributive share of non-ECI is positive, this fraction is treated as zero. If the specified foreign partner's distributive share of non-ECI is negative or zero and its distributive share of ECI is positive, this fraction is treated as one. If the specified foreign partner's distributive share of ECI and distributive share of non-ECI are both negative, the numerator of this fraction is its distributive share of non-ECI and the denominator is its distributive share of partnership items of income, gain, deduction, and loss.

(iii) *Distributive share of ECI.* The term *distributive share of ECI* means the net amount of the specified foreign partner's distributive share of partnership items of income, gain, deduction, and loss that are ECI.

(iv) *Distributive share of non-ECI.* The term *distributive share of non-ECI* means the net amount of the specified foreign partner's distributive share of partnership items of income, gain, deduction, and loss that are not ECI.

(2) *Characterization of excess business interest expense*—(i) *Allocable ECI excess BIE.* The portion of excess business interest expense allocated to a specified foreign partner from a partnership pursuant to § 1.163(j)–6(f)(2) or paragraph (e)(2) of this section that is ECI (*allocable ECI excess BIE*) is equal to the excess, if any, of allocable ECI BIE over allocable ECI deductible BIE.

(ii) *Allocable non-ECI excess BIE.* The portion of excess business interest expense allocated to a specified foreign partner from a partnership pursuant to § 1.163(j)–6(f)(2) or paragraph (e)(2) of this section that is not ECI (*allocable non-ECI excess BIE*) is equal to the excess, if any, of allocable non-ECI BIE over allocable non-ECI deductible BIE.

(3) *Characterization of deductible business interest expense*—(i) *In general.* The portion of deductible business interest expense, if any, that is allocated to a specified foreign partner from a partnership pursuant to § 1.163(j)–6(f)(2) that is ECI (*allocable ECI deductible BIE*) is equal to the sum of the amounts described in paragraphs (c)(3)(ii)(A)(*1*)(*i*) and (c)(3)(ii)(B)(*1*) of this section. The portion of deductible business interest expense, if any, that is allocated to a specified foreign partner from a partnership pursuant to § 1.163(j)–6(f)(2) that is not ECI (*allocable non-ECI deductible BIE*) is equal to the sum of the amounts described in paragraphs (c)(3)(ii)(A)(*1*)(*ii*) and (c)(3)(ii)(B)(*2*) of this section.

(ii) *Allocation between allocable ECI deductible BIE and allocable non-ECI deductible BIE.* For purposes of paragraph (c)(3)(i) of this section—

(A) *Allocation to hypothetical deductible amounts*—(*1*) *In general.* Subject to paragraph (c)(3)(ii)(A)(*2*) of this section, deductible business interest expense that is allocated to the specified foreign partner from the partnership pursuant to § 1.163(j)–6(f)(2) is allocated pro rata to—

(*i*) Hypothetical partnership ECI deductible BIE; and

(*ii*) Hypothetical partnership non-ECI deductible BIE.

(*2*) *Limitation.* The amount allocated to hypothetical partnership ECI deductible BIE in paragraph (c)(3)(ii)(A)(*1*)(*i*) of this section cannot exceed the lesser of hypothetical partnership ECI deductible BIE or allocable ECI BIE, and the amount allocated to hypothetical partnership non-ECI deductible BIE in paragraph (c)(3)(ii)(A)(*1*)(*ii*) of this section cannot exceed the lesser of hypothetical partnership non-ECI deductible BIE or allocable non-ECI BIE.

(B) *Allocation of remaining deductible amounts.* Deductible business interest expense that is allocated to the specified foreign partner from the partnership pursuant to § 1.163(j)–6(f)(2) in excess of the amount allocated in paragraph (c)(3)(ii)(A) of this section, if any, is allocated pro rata to—

(*1*) Allocable ECI BIE, reduced by the amount described in paragraph (c)(3)(ii)(A)(*1*)(*i*) of this section; and

(*2*) Allocable non-ECI BIE, reduced by the amount described in paragraph (c)(3)(ii)(A)(*1*)(*ii*) of this section.

(iii) *Hypothetical partnership deductible business interest expense*—(A) *Hypothetical partnership ECI deductible BIE.* The term *hypothetical partnership ECI deductible BIE* means the deductible business interest expense of the partnership, as defined in § 1.163(j)–6(b)(5), determined by only taking into account the specified foreign partner's allocable share of items that are ECI (including by reason of paragraph (f)(1)(iii) of this section).

(B) *Hypothetical partnership non-ECI deductible BIE.* The term *hypothetical partnership non-ECI deductible BIE* means the deductible business interest expense of the partnership, as defined in § 1.163(j)–6(b)(5), determined by only taking into account the specified foreign partner's allocable share of items that are not ECI (including by reason of paragraph (f)(1)(iii) of this section).

(4) *Characterization of excess business interest income*—(i) *In general.* The portion of excess business interest income allocated to a specified foreign partner from a partnership pursuant to § 1.163(j)–6(f)(2) that is ECI is equal to the specified foreign partner's allocation of excess business interest income from the partnership multiplied by its specified BII ratio with respect to the partnership, and the remainder is not ECI.

(ii) *Specified BII ratio.* The term *specified BII ratio* means the ratio of the specified foreign partner's allocable ECI BII to allocable business interest income (determined under § 1.163(j)–6(f)(2)(ii)).

(iii) *Allocable ECI BII.* The term *allocable ECI BII* means the specified foreign partner's allocable BII, as determined under § 1.163(j)–6(f)(2)(ii), computed by only taking into account income that is ECI.

(5) *Rules for determining ECI.* Except as described in paragraph (f)(1) of this section, if the determination as to whether partnership items are ECI is made by a direct or indirect partner, rather than the partnership itself, then for purposes of this paragraph (c), the partnership must use a reasonable method to characterize such items as ECI or as not ECI.

(d) *Characterization of disallowed business interest expense by a relevant foreign corporation with ECI*—(1) *Scope.* A relevant foreign corporation that has ECI and disallowed business interest expense for a taxable year determines the portion of its disallowed business interest expense and deductible business interest expense that is characterized as ECI or as not ECI under this paragraph (d). A relevant foreign corporation that is a specified foreign partner also applies the rules in paragraph (c) of this section. See also § 1.163(j)–7(f) for rules regarding CFC group members with ECI.

(2) *Characterization of disallowed business interest expense*—(i) *FC ECI disallowed BIE.* For purposes of this section, the portion of disallowed business interest expense of a relevant foreign corporation that is ECI (*FC ECI disallowed BIE*) is equal to the excess, if any, of FC ECI BIE over FC ECI deductible BIE.

(ii) *FC non-ECI disallowed BIE.* For purposes of this section, the portion of disallowed business interest expense of a relevant foreign corporation that is not ECI (*FC non-ECI disallowed BIE*) is equal to the excess, if any, of FC non-ECI BIE over FC non-ECI deductible BIE.

(3) *Characterization of deductible business interest expense*—(i) *In general.* The portion of deductible business interest expense, if any, that is ECI (*FC ECI deductible BIE*) is equal to the sum of the amounts described in paragraphs (d)(3)(ii)(A)(*1*)(*i*) and (d)(3)(ii)(B)(*1*) of this section. The portion of deductible business interest expense, if any, that is allocable to income that is not ECI (*FC non-ECI deductible BIE*) is equal to the sum of the amounts described in paragraphs (d)(3)(ii)(A)(*1*)(*ii*) and (d)(3)(ii)(B)(*2*) of this section.

(ii) *Allocation between FC ECI deductible BIE and FC non-ECI deductible BIE.* For purposes of paragraph (d)(3)(i) of this section—

(A) *Allocation to hypothetical deductible amounts*—(*1*) *In general.* Subject to paragraph (d)(3)(ii)(A)(*2*) of this section, deductible business interest expense is allocated pro rata to—

(*i*) Hypothetical FC ECI deductible BIE; and

(*ii*) Hypothetical FC non-ECI deductible BIE.

(*2*) *Limitation.* The amount allocated to hypothetical FC ECI deductible BIE in paragraph (d)(3)(ii)(A)(*1*)(*i*) of this section cannot exceed the lesser of hypothetical FC ECI deductible BIE or FC ECI BIE, and the amount allocated to hypothetical FC non-ECI deductible BIE in paragraph (d)(3)(ii)(A)(*1*)(*ii*) of this section cannot exceed the lesser of hypothetical FC non-ECI deductible BIE or FC non-ECI BIE.

(B) *Allocation of remaining deductible amounts.* Deductible business interest expense in excess of the amount allocated in paragraph (d)(3)(ii)(A) of this section, if any, is allocated pro rata to—

(*1*) FC ECI BIE, reduced by the amount described in paragraph (d)(3)(ii)(A)(*1*)(*i*) of this section; and

(*2*) FC non-ECI BIE, reduced by the amount described in paragraph (d)(3)(ii)(A)(*1*)(*ii*) of this section.

(iii) *Hypothetical FC deductible business interest expense*—(A) *Hypothetical FC ECI deductible BIE.* The term *hypothetical FC ECI deductible BIE* means the deductible business interest expense of the relevant foreign corporation determined by only taking into account its items that are ECI.

(B) *Hypothetical FC non-ECI deductible BIE.* The term *hypothetical FC non-ECI deductible BIE* means the deductible business interest expense of the relevant foreign corporation determined by only taking into account its items that are not ECI.

(e) *Rules regarding disallowed business interest expense*—(1) *Retention of character in a succeeding taxable year.* Disallowed business interest expense of a specified foreign person or a relevant foreign corporation for a taxable year (including excess business interest expense allocated to a specified foreign partner under § 1.163(j)–6(f)(2) or paragraph (e)(2) of this section) that is ECI or is not ECI retains its character as ECI or as not ECI in a succeeding taxable year.

(2) *Deemed allocation of excess business interest expense of a partnership to a specified foreign partner.* For purposes of this paragraph (e) and paragraphs (c)(2), (g)(3), and (g)(7) of this section, a specified foreign partner's allocable share of business interest expense is deemed to include its allocable share of excess business interest expense of a partnership in which it is a direct or indirect partner. For purposes of this paragraph (e)(2), a specified foreign partner's allocable share of excess business interest

expense of a partnership in which it is a direct or indirect partner is determined as if the excess business interest expense of the partnership were deductible in the taxable year in which the interest expense is first paid or accrued.

(3) *Ordering rule for conversion of excess business interest expense to business interest expense paid or accrued by a partner.* A specified foreign partner's allocable share of excess business interest expense (determined under § 1.163(j)–6(f)(2) or paragraph (e)(2) of this section) is treated as business interest expense paid or accrued under § 1.163(j)–6(g)(2)(i) in the order of the taxable years in which the excess business interest expense arose, and pro rata between allocable ECI excess BIE and allocable non-ECI excess BIE that arose in the same taxable year. This paragraph (e)(3) applies before application of paragraph (b)(3) of this section.

(4) *Allocable ECI excess BIE and allocable non-ECI excess BIE retains its character when treated as business interest expense paid or accrued in a succeeding taxable year.* If excess business interest expense of a partnership in which a specified foreign partner is a direct or indirect partner is treated as business interest expense paid or accrued by the specified foreign partner or a partnership in which it is a direct or indirect partner under § 1.163(j)–6(g)(2)(i), then allocable ECI excess BIE is treated as business interest expense allocable to ECI and allocable non-ECI excess BIE is treated as business interest expense allocable to income that is not ECI.

(f) *Coordination of the application of section 163(j) with § 1.882–5 and similar provisions and with the branch profits tax*—(1) *Coordination of section 163(j) with § 1.882–5 and similar provisions*—(i) *Ordering rule.* A foreign corporation first determines its business interest expense allocable to ECI under § 1.882–5 or any other relevant provision (*§ 1.882–5 and similar provisions*) before applying section 163(j) to the foreign corporation. If a foreign corporation has a disallowed business interest expense carryforward from a taxable year, then none of that business interest expense is taken into account for purposes of determining business interest expense under § 1.882–5 and similar provisions in a succeeding taxable year.

(ii) *Treatment of excess business interest expense.* For purposes of applying § 1.882–5 and similar provisions, the business interest expense of a specified foreign partner that is a direct or indirect partner in a partnership is determined without regard to the application of section 163(j) to the partnership. As a result, for purposes of applying § 1.882–5 and similar provisions, the specified foreign partner's share of business interest expense on liabilities of a partnership in which it is a direct or indirect partner is determined as if any excess business interest expense of the partnership (determined under § 1.163(j)–6(f)(2) or paragraph (e)(2) of this section) were deductible in the taxable year in which the business interest expense is first paid or accrued and not in a succeeding taxable year.

(iii) *Attribution of certain § 1.882–5 interest expense among the foreign corporation and its partnership interests*—(A) *In general.* If a foreign corporation is a specified foreign partner in one or more partnerships, then, for purposes of section 163(j) and the section 163(j) regulations, interest expense determined under § 1.882–5(b) through (d) or § 1.882–5(e) (*§ 1.882–5 three-step interest expense*) is treated as attributable to liabilities of the foreign corporation or the foreign corporation's share of liabilities of each partnership in accordance with paragraphs (f)(1)(iii)(B) and (f)(1)(iii)(C) of this section. Accordingly, the portion of the § 1.882–5 three-step interest expense attributable to liabilities of the foreign corporation described in this paragraph (f)(1)(iii) is subject to section 163(j) and the section 163(j) regulations at the level of the foreign corporation. The portion of the § 1.882–5 three-step interest expense interest attributable to liabilities of a partnership described in this paragraph (f)(1)(iii) is subject to section 163(j) and the section 163(j) regulations at the partnership-level. See § 1.163(j)–6. This paragraph (f)(1)(iii) merely characterizes interest expense of the foreign corporation and its partnership interests as ECI or not ECI. It does not change the amount of interest expense of the foreign corporation or its partnership interests.

(B) *Attribution of interest expense on U.S. booked liabilities.* The § 1.882–5 three-step interest expense is treated as attributable, pro rata, to interest expense on U.S. booked liabilities of a foreign corporation, determined under § 1.882–5(d)(2)(ii)–(iii) or its interest expense on its share of U.S. booked liabilities of a partnership, determined under § 1.882–5(d)(2)(vii), as applicable, to the extent thereof (without regard to whether the foreign corporation uses the method described in § 1.882–5(b) through (d) or the method described in § 1.882–5(e) for purposes of determining § 1.882–5 interest expense).

(C) *Attribution of excess § 1.882–5 three-step interest expense*—(*1*) *In general.* The § 1.882–5 three-step interest expense in excess of interest expense attributable to U.S. booked liabilities described in § 1.882–5(d)(2), if any (*excess § 1.882–5 three-step interest expense*), is treated as attributable to liabilities of the foreign corporation or the foreign corporation's allocable share of liabilities of one or more partnerships, in accordance with paragraphs (f)(1)(iii)(C)(*2*) and (f)(1)(iii)(C)(*3*) of this section, subject to the limitation in paragraph (f)(1)(iii)(C)(*4*) of this section. For purposes of this paragraph (f)(1)(iii)(C), the term ''U.S. assets'' means U.S. assets described in § 1.882–5(b).

(*2*) *Attribution of excess § 1.882–5 three-step interest expense to the foreign corporation.* Excess § 1.882–5 three-step interest expense is treated as attributable to interest expense on liabilities of the foreign corporation (and not its partnership interests) in proportion to its U.S. assets other than its partnership interests over all of its U.S. assets.

(*3*) *Attribution of excess § 1.882–5 three-step interest expense to partnerships*—(*i*) *In general.* Excess § 1.882–5 three-step interest expense is treated as attributable to interest expense on the foreign corporation's direct or indirect allocable share of liabilities of a partnership in proportion to the portion of the partnership interest that is treated as a U.S. asset under paragraph (f)(1)(iii)(C)(*3*)(*ii*) of this section over all of the foreign corporation's U.S. assets.

(*ii*) *Direct and indirect partnership interests.* If a foreign corporation owns an interest in a partnership that does not own an interest in any other partnerships, the portion of the partnership interest that is a U.S. asset is determined under § 1.882–5(b). If a foreign corporation owns an interest in a partnership (the top-tier partnership) that owns an interest in one or more other partnerships, directly or indirectly (the lower-tier partnerships), the portion of the foreign corporation's direct or indirect interest in the top-tier partnership and lower-tier partnerships that is a U.S. asset is determined by re-attributing the portion of the top-tier partnership interest that is a U.S. asset, as determined under § 1.882–5(b), among the foreign corporation's direct interest in the top-tier partnership and indirect interests in each lower-tier partnership in proportion to their contribution to the portion of the foreign corporation's interest in the upper-tier partnership that is a U.S. asset. Each partnership interest's contribution is determined based on a reasonable method consistent with the method used to determine the portion of the top-tier partnership interest that is a U.S. asset under § 1.882–5(b).

(*4*) *Limitation on attribution of excess § 1.882–5 three-step interest expense.* The portion of excess § 1.882–5 three-step interest expense attributable to a foreign corporation under paragraph (f)(1)(iii)(C)(*2*) of this section or to a partnership under paragraph (f)(1)(iii)(C)(*2*) or (f)(1)(iii)(C)(*3*) of this section, as applicable, is limited to interest on liabilities of the foreign corporation or the foreign corporation's allocable share of liabilities of the partnership, reduced by the sum of the amounts of interest expense on its U.S. booked liabilities described in § 1.882–5(d)(2) and interest expense on liabilities described in § 1.882–5(a)(1)(ii)(A) or (B) (regarding direct allocations of interest expense). The portion of any excess § 1.882–5 three-step interest expense that would be treated as attributable to the foreign corporation or a partnership interest, as applicable, but for this paragraph (f)(1)(iii)(C)(*4*) is re-attributable in accordance with the rules and principles of this paragraph (f)(1)(iii)(C). The portion of any excess § 1.882–5 three-step interest expense that cannot be re-attributed under the rules of (f)(1)(iii)(C)(*1*) through (*3*) of this section because of the application of the first sentence of this paragraph (f)(1)(iii)(C)(*4*) is attributable, first to interest on liabilities of the foreign corporation, and then, pro rata, to the foreign corporation's allocable share of interest on liabilities of its direct or indirect partnership interests, to the extent such attribution is not in excess of the limitation described in this paragraph (f)(1)(iii)(C)(*4*), and without regard to whether the foreign corporation or its partnership interests have U.S. assets.

(2) *Coordination with the branch profits tax.* The disallowance and carryforward of business interest expense under § 1.163(j)–2(b) and (c) will not affect the computation of the U.S. net equity of a foreign corporation, as defined in § 1.884–1(c).

(g) *Definitions.* The following definitions apply for purposes of this section.

(1) *§ 1.882–5 and similar provisions.* The term *§ 1.882–5 and similar provisions* has the meaning provided in paragraph (f)(1)(i) of this section.

(2) *§ 1.882–5 three-step interest expense.* The term *§ 1.882–5 three-step interest expense* has the meaning provided in paragraph (f)(1)(iii)(A) of this section.

(3) *Allocable ECI BIE.* The term *allocable ECI BIE* means, with respect to a partnership, the specified foreign partner's allocable share of the partnership's business interest expense that is ECI, taking into account the application of paragraph (e)(2) of this section.

(4) *Allocable ECI BII.* The term *allocable ECI BII* has the meaning provided in paragraph (c)(4)(ii) of this section.

(5) *Allocable ECI deductible BIE.* The term *allocable ECI deductible BIE* has the meaning provided in paragraph (c)(3)(i) of this section.

(6) *Allocable ECI excess BIE.* The term *allocable ECI excess BIE* has the meaning provided in paragraph (c)(2)(i) of this section.

(7) *Allocable non-ECI BIE.* The term *allocable non-ECI BIE* means, with respect a partnership, the specified foreign partner's allocable share of the partnership's business interest expense that is not ECI, taking into account the application of paragraph (e)(2) of this section.

(8) *Allocable non-ECI deductible BIE.* The term *allocable non-ECI deductible BIE* has the meaning provided in paragraph (c)(3)(i) of this section.

(9) *Allocable non-ECI excess BIE.* The term *allocable non-ECI excess BIE* has the meaning provided in paragraph (c)(2)(ii) of this section.

(10) *Distributive share of ECI.* The term *distributive share of ECI* has the meaning provided in paragraph (c)(1)(iii) of this section.

(11) *Distributive share of non-ECI.* The term *distributive share of non-ECI* has the meaning provided in paragraph (c)(1)(iv) of this section.

(12) *Effectively connected income.* The term *effectively connected income* (or *ECI*) means income or gain that is ECI, as defined in § 1.884–1(d)(1)(iii), and deduction or loss that is allocable to, ECI, as defined in § 1.884–1(d)(1)(iii).

(13) *Excess § 1.882–5 three-step interest expense.* The term *excess § 1.882–5 three-step interest expense* has the meaning provided in paragraph (f)(1)(iii)(C)(*1*) of this section.

(14) *FC ECI BIE.* The term *FC ECI BIE* means, with respect to a relevant foreign corporation and a taxable year, business interest expense that is ECI, determined without regard to the application of section 163(j) and the section 163(j) regulations except for the application of paragraph (f)(1)(iii) of this section.

(15) *FC ECI deductible BIE.* The term *FC ECI deductible BIE* has the meaning provided in paragraph (d)(3)(i) of this section.

(16) *FC ECI disallowed BIE.* The term *FC ECI disallowed BIE* has the meaning provided in paragraph (d)(2)(i) of this section.

(17) *FC non-ECI BIE.* The term *FC non-ECI BIE* means, with respect to a relevant foreign corporation and a taxable year, business interest expense that is not ECI, determined without regard to the application of section 163(j) and the section 163(j) regulations except for the application of paragraph (f)(1)(iii) of this section.

(18) *FC non-ECI deductible BIE.* The term *FC non-ECI deductible BIE* has the meaning provided in paragraph (d)(3)(i) of this section.

(19) *FC non-ECI disallowed BIE.* The term *FC non-ECI disallowed BIE* has the meaning provided in paragraph (d)(2)(ii) of this section.

(20) *Hypothetical partnership ECI deductible BIE.* The term *hypothetical partnership ECI deductible BIE* has the meaning provided in paragraph (c)(3)(iii)(A) of this section.

(21) *Hypothetical partnership non-ECI deductible BIE.* The term *hypothetical partnership non-ECI deductible BIE* has the meaning provided in paragraph (c)(3)(iii)(B) of this section.

(22) *Hypothetical FC ECI deductible BIE.* The term *hypothetical FC ECI deductible BIE* has the meaning provided in paragraph (d)(3)(iii)(A) of this section.

(23) *Hypothetical FC non-ECI deductible BIE.* The term *hypothetical FC non-ECI deductible BIE* has the meaning provided in paragraph (d)(3)(iii)(B) of this section.

(24) *Specified ATI ratio.* The term *specified ATI ratio* has the meaning provided in paragraph (c)(1)(ii) of this section.

(25) *Specified BII ratio.* The term *specified BII ratio* has the meaning provided in paragraph (c)(4)(ii) of this section.

(26) *Specified foreign partner.* The term *specified foreign partner* means, with respect to a partnership that has ECI, a direct or indirect partner that is a specified foreign person or a relevant foreign corporation.

(27) *Specified foreign person.* The term *specified foreign person* means a nonresident alien individual, as defined in section 7701(b) and the regulations under section 7701(b), or a foreign corporation other than a relevant foreign corporation.

(28) *Successor.* The term *successor* includes, with respect to a foreign corporation, the acquiring corporation in a transaction described in section 381(a) in which the foreign corporation is the distributor or transferor corporation.

(h) *Examples.* The following examples illustrate the application of this section. For all examples, assume that all referenced interest expense is deductible but for the application of section 163(j), the small business exemption under § 1.163(j)–2(d) is not available, no entity is engaged in an excepted trade or business, no business interest expense is floor plan financing interest expense, all entities have the same taxable year, all entities use the U.S. dollar as their functional currency, no foreign corporation is a relevant foreign corporation, all relevant taxable years begin after December 31, 2020, and, for purposes of computing ATI, none of the adjustments described in § 1.163(j)–1(b) are relevant other than the adjustment for business interest expense.

(1) *Example 1. Limitation on business interest deduction of a foreign corporation*—(i) *Facts.* FC, a foreign corporation, has $100x of gross income that is ECI. FC has $60x of other income which is not ECI. FC has total expenses of $100x, of which $50x is business interest expense. Assume that FC has $30x of § 1.882–5 three-step interest expense. Under section 882(c) and the regulations, FC has $40x of other expenses that are ECI, none of which are business interest expense. FC does not have any business interest income. All amounts described in this paragraph (h)(1)(i) are with respect to a single taxable year of FC.

(ii) *Analysis.* FC is a specified foreign person under paragraph (g)(27) of this section. The amount of FC's business interest expense that is disallowed for the taxable year is determined under § 1.163(j)–2(b) with respect to business interest expense described in paragraph (b)(3) of this section. Under paragraph (b)(3) of this section, FC has business interest expense of $30x. Under paragraph (b)(2) of this section, FC has ATI of $60x ($100x − $40x). Accordingly, FC's section 163(j) limitation is $18x ($60x × 30 percent). Because FC's business interest expense ($30x) that is ECI exceeds the section 163(j) limitation ($18x), FC may only deduct $18x of business interest expense. Under § 1.163(j)–2(c), the remaining $12x is disallowed business interest expense carryforward, and under paragraph (f)(1)(i) of this section, the $12x is not taken into account for purposes of applying § 1.882–5 in the succeeding taxable year.

(2) *Example 2. Use of a disallowed business interest expense carryforward*—(i) *Facts.* The facts are the same as in *Example 1* in paragraph (h)(1)(i) of this section except that for the taxable year FC has $300x of gross income that is all ECI. Furthermore, assume that for the taxable year FC has a disallowed business interest expense carryforward of $25x with respect to business interest expense described in paragraph (b)(3) of this section.

(ii) *Analysis.* Under paragraph (f)(1)(i) of this section, FC's $25x of disallowed business interest expense carryforward is not taken into account for purposes of determining FC's interest expense under § 1.882–5 for the taxable year. Therefore, FC has $30x of § 1.882–5 three-step interest expense. Under paragraph (b)(2) of this section, FC has ATI of $260x ($300x of gross income reduced by $40 of expenses other than business interest expense). Accordingly, FC's section 163(j) limitation is $78x ($260x × 30 percent). Because FC's business interest expense ($55x) does not exceed the section 163(j) limitation ($78x), FC may deduct all $55x of business interest expense.

(3) *Example 3. Foreign corporation is engaged in a U.S. trade or business and is also a specified foreign partner*—(i) *Facts.* FC, a foreign corporation, owns a 50-percent interest in ABC, a partnership that has ECI. In addition to owning a 50-percent interest in ABC, FC conducts a separate business that is engaged in a trade or business in the United States, Business Y. Business Y produces $65x of taxable income before taking into account business interest expense and has U.S. assets with an adjusted basis of $300x, business interest expense of $15x on $160x of liabilities, and no business interest income. All of the liabilities of Business Y are U.S. booked liabilities for purposes of § 1.882–5(d). FC also has various foreign operations, some of which have U.S. dollar denominated debt. ABC has two lines of business, Business S and Business T. FC is allocated 50 percent of all items of income and expense of Business S and Business T. Business S produces $140x of taxable income before taking into account business interest expense, and Business T produces $80x of taxable income before taking into account business interest expense. Business S has business interest expense of $20x on $400x of liabilities and no business interest income. Business T has business interest expense of $10x on $150x of liabilities and no business interest income. With respect to FC, only Business S produces ECI. FC has an outside basis of $600x in the portion of its ABC partnership interest that is a U.S. asset for purposes of § 1.882–5(b), step 1. All of the liabilities of Business S are U.S. booked liabilities for purposes of § 1.882–5(d). FC computes its interest expense under the three-step method described in § 1.882–5(b) through (d) and for purposes of § 1.882–5(c), step 2, FC uses the fixed ratio of 50 percent described in § 1.882–5(c)(4) for taxpayers that are neither a bank nor an insurance company. Under § 1.882–5(d)(5)(ii), FC's interest rate on excess U.S. connected liabilities is 5 percent. For the taxable year, assume FC has total interest expense of $100x for purposes of § 1.882–5(a)(3). All amounts described in this paragraph (h)(3)(i) are with respect to a single taxable year of FC or ABC, as applicable.

(ii) *Analysis*—(A) *Application of § 1.882–5 to FC.* FC is a specified foreign person under paragraph (g)(27) of this section and a specified foreign partner under paragraph (g)(26) of this section. Under paragraph (f)(1) of this section, FC first determines its § 1.882–5 three-step interest expense and then applies section 163(j). Under § 1.882–5(b), step 1, FC has U.S. assets of $900x ($600x of basis in the portion of its ABC partnership interest that is a U.S. asset determined using the asset method described in § 1.884–1(d)(3)(ii) + $300x basis in U.S. assets of Business Y). Under § 1.882–5(c), step 2, applying the 50-percent fixed ratio described in § 1.882–5(c)(4), FC has U.S. connected liabilities of $450x ($900x × 50 percent). Under § 1.882–5(d), step 3, FC has U.S. booked liabilities of $360x ($200x attributable to its 50-percent share of Business S liabilities of ABC + $160x of Business Y liabilities) and interest on U.S. booked liabilities of $25x ($10x attributable to its 50-percent share of $20x interest expense of Business S + $15x of Business Y interest expense). FC has excess U.S. connected liabilities of $90x ($450x − $360x) and under § 1.882–5(d)(5) has interest expense on excess U.S. connected liabilities of $4.50x ($90x × 5 percent), which is excess § 1.882–5 three-step interest expense. FC's § 1.882–5 three-step interest expense is $29.50x ($25x + $4.50x).

(B) *Attribution of § 1.882–5 business interest expense between FC and ABC.* Under paragraph (f)(1)(iii) of this section, FC's § 1.882–5 three-step interest expense is attributable to interest on its liabilities or on its share of ABC liabilities. Under paragraph (f)(1)(iii)(B), FC's § 1.882–5 three-step interest expense of $29.50x is first attributable to $15 of interest expense on FC's (Business Y) U.S. booked liabilities and $10x of interest expense on FC's share of U.S. booked liabilities of ABC. Under paragraph (f)(1)(iii)(C)(*2*) of this section, of the excess § 1.882–5 three-step interest expense of $4.50x ($29.50x − $15x − $10x), 66.67 percent ($600x of basis in the portion of the ABC partnership interest that is a U.S. asset/$900x of total U.S. assets), or $3.00x, is attributable to interest expense on FC's share of liabilities of ABC and 33.33 percent ($300x U.S. assets other than partnership interests/$900x of total U.S. assets), or $1.50x, is attributable to interest expense on liabilities of FC. As a result, $16.50x of business interest expense ($15x + $1.50x) is attributed to FC and $13x of business interest expense ($10x + $3x) is attributed to ABC. The limitation under paragraph (f)(1)(iii)(C)(*4*) of this section does not change the result described in the preceding sentence. Specifically, under paragraph (f)(1)(iii)(C)(*4*) of this section, the amount attributed to ABC (tentatively, $3.00x) is limited to $5x (FC's 50-percent share of the $30x of business interest expense of ABC or $15x, reduced by FC's 50-percent share of the $20x of business interest expense on U.S. booked liabilities of Business S), and the amount attributed to FC (tentatively, $1.50x) is limited to $70x (FC's business interest expense of $100x, reduced by $15x of business interest expense on U.S. booked liabilities of Business Y and its $15x allocable share of ABC's business interest expense).

(C) *Application of the section 163(j) limitation to ABC.* Under § 1.163(j)–6(a), ABC computes a section 163(j) limitation at the partnership level. ABC has business interest expense of $30x ($20x from Business S and $10x from Business T). Under § 1.163(j)–6(d), ABC has ATI of $220x ($140 + $80). Under § 1.163(j)–2(b), ABC's section 163(j) limitation is $66x ($220x × 30 percent). Because ABC's business interest expense ($30x) does not exceed the section 163(j) limitation ($66x), all of ABC's business interest expense is deductible for the taxable year.

(D) *Excess taxable income of ABC.* Under § 1.163(j)–1(b)(15), ABC has excess taxable income of $120x ($220x × ($36x/$66x)). Under § 1.163(j)–6(f)(2), FC is allocated 50 percent of the $120x of ABC's excess taxable income or $60x of allocable excess taxable income. Under paragraph (c)(1) of this section, the amount of the allocable excess taxable income of $60x that is ECI is equal to FC's allocable excess taxable income multiplied by the specified ATI ratio. Under paragraph (c)(1)(iii) of this section, FC's distributive share of ECI of ABC is $57x (FC's 50-percent share of $140x (Business S income computed without regard to business interest expense) or $70x–$13x of business interest expense that is ECI). Under paragraph (c)(1)(iv) of this section, FC's distributive share of non-ECI of ABC is $38x (FC's 50-percent share of $80x (Business T income computed without regard to business interest expense) or $40x–$2x of business interest expense that is not ECI). FC's distributive share of partnership items of income, gain, deduction, and loss of ABC is $95x ($57x distributive share of ECI and $38x distributive share of non-ECI). Because both FC's distributive share of ECI and distributive share of non-ECI are positive, under paragraph (c)(1)(ii) of this section, the specified ATI ratio is 60 percent ($57x distributive share of ECI/$95x distributive share of partnership items of income, gain, deduction, and loss of ABC). As a result, the amount of FC's allocable excess taxable income from ABC that is ECI is $36x ($60 of allocable excess taxable income × 60 percent specified ATI ratio).

(E) *Application of section 163(j) to FC.* Under paragraph (b)(3) of this section, FC's business interest expense is $16.50x. Under § 1.163(j)–6(e)(1), FC's ATI is determined under § 1.163(j)–1(b)(1) without regard to FC's distributive share of any items of income, gain, deduction, or loss of ABC. Under paragraph (b)(2) of this section, FC's ATI is $101x ($65x of ECI from Business Y + $36x of allocable excess taxable income from ABC that is ECI). FC's section 163(j) limitation is $30.30x ($101x × 30 percent). Because FC's business interest expense ($16.50x) is less than FC's section 163(j) limitation ($30.30x) and all of its share of ABC's business interest expense that is allocable to ECI ($13x) is deductible, FC may deduct all $29.50x of § 1.882–5 three-step interest expense determined under paragraph (h)(3)(ii)(A) of this section.

(4) *Example 4. Specified foreign partner with excess business interest expense from a partnership*—(i) *Facts*—(A) *In general.* FC, a foreign corporation, owns a 50-percent interest in ABC, a partnership that has ECI. In addition to owning a 50-percent interest in ABC, FC conducts a separate business that is engaged in a trade or business in the United States, Business Y. Business Y produces $56x of taxable income before taking into account business interest expense and has U.S. assets with an adjusted basis of $800x, business interest expense of $16x on $200x of liabilities, and no business interest income. All of the liabilities of Business Y are U.S. booked liabilities for purposes of § 1.882–5(d). FC also has various foreign operations, some of which have U.S. dollar denominated debt.

(B) *ABC Partnership.* ABC has two lines of business, Business S and Business T, and owns a 50-percent interest in DEF, a partnership. FC is allocated 50 percent of all items of income and expenses of Business S and Business T and ABC's allocable share of items from partnership DEF. Business S produces $80x of taxable income before taking into account business interest expense, and Business T produces $90x of taxable income before taking into account business interest expense. Business S has business interest expense of $30x on $500x of liabilities and no business interest income. Business T has business interest expense of $50x on $500x of liabilities and no business interest income. With respect to FC, only Business S produces ECI. All of the liabilities of Business S are U.S. booked liabilities for purposes of § 1.882–5(d).

(C) *DEF Partnership.* DEF has two lines of business, Business U and Business V. ABC is allocated 50 percent of all items of income and expenses of Business U and Business V. Business U produces $100x of taxable income before taking into account business interest expense and Business V produces $140x of taxable income before taking into account business interest expense. Business U has business interest expense of $40x on $600x of liabilities and no business interest income. Business V has business interest expense of $60x on $600x of liabilities and no business interest income. With respect to FC, only Business U produces ECI. All of the liabilities of Business U are U.S. booked liabilities for purposes of § 1.882–5(d).

(D) *Section 1.882–5.* FC has an outside basis of $600x in the portion of its ABC partnership interest that is a U.S. asset for purposes of § 1.882–5(b), step 1, determined using the asset method described in § 1.884–1(d)(3)(ii). For purposes of § 1.884–1(d)(3)(ii), ABC has a total basis of $500 in assets that would be treated as U.S. assets if ABC were a foreign corporation, including a basis of $250x in the portion of its interest in DEF partnership interest that would be treated as a U.S. asset if ABC were a foreign corporation. FC computes its interest expense under the three-step method described in § 1.882–5(b) through (d), and for purposes of § 1.882–5(c), step 2, FC uses the fixed ratio of 50 percent described in § 1.882–5(c)(4) for taxpayers that are neither a bank nor an insurance company. FC has total interest expense of $100x for purposes of § 1.882–5(a)(3). Under § 1.882–5(d)(5)(ii), FC's interest rate on excess U.S. connected liabilities is 6 percent. All amounts described in this paragraph (h)(4)(i) are with respect to a single taxable year of FC, ABC, or DEF, as applicable.

(ii) *Analysis*—(A) *Application of § 1.882–5 to FC.* FC is a specified foreign person under paragraph (g)(27) of this section and a specified foreign partner under paragraph (g)(26) of this section. Under paragraph (f)(1) of this section, FC first determines its § 1.882–5 three-step interest expense and then applies section 163(j). Under § 1.882–5(b), step 1, FC has U.S. assets of $1400x ($600x of basis in the portion of its ABC partnership interest that is a U.S. asset + $800x basis in U.S. assets of Business Y). Under § 1.882–5(c), step 2, applying the 50-percent fixed ratio described in § 1.882–5(c)(4), FC has U.S. connected liabilities of $700x ($1400x × 50 percent). Under § 1.882–5(d), step 3, FC has U.S. booked liabilities of $600x ($250x attributable to its 50-percent share of Business S liabilities of ABC + $150x attributable to its indirect 25-percent share of Business U liabilities of DEF + $200x of Business Y liabilities), and interest on U.S. booked liabilities of $41x ($15x attributable to its 50-percent share of $30x interest expense of Business S + $10x attributable to its 25-percent share of $40 interest expense of Business U + $16x of Business Y interest expense). FC has excess U.S. connected liabilities of $100x ($700x − $600x) and under § 1.882–5(d)(5), interest expense on excess U.S. connected liabilities of $6x ($100x × 6 percent), which is excess § 1.882–5 three-step interest expense. FC's § 1.882–5 three-step interest expense is $47x ($41x + $6x).

(B) *Attribution of certain § 1.882–5 business interest expense among FC, ABC, and DEF.* Under paragraph (f)(1)(iii) of this section, FC's § 1.882–5 three-step interest expense is attributable to interest on its liabilities or on its share of ABC and DEF's liabilities. Under paragraph (f)(1)(iii)(B) of this section, FC's § 1.882–5 three-step interest expense of $47x is first attributable to $16 of interest expense on FC's U.S. booked liabilities, $15x of interest expense on FC's share of U.S. booked liabilities of ABC, and $10x of interest expense on FC's share of U.S. booked liabilities of DEF. Under paragraph (f)(1)(iii)(C)(*2*) of this section, of the excess § 1.882–5 three-step interest expense of $6x ($47x − $16x − $15x − $10x), 42.86 percent ($600x of basis in the portion of the ABC partnership interest that is a U.S. asset/ $1400x of total U.S. assets) or $2.57x is attributable to interest expense on FC's share of liabilities of ABC (and its partnership interests), and 57.14 percent ($800x U.S. assets other than partnership interests/ $1400x of total U.S. assets) or $3.43x is attributable to interest expense on liabilities of FC. Under paragraph (f)(1)(iii)(C)(*3*) of this section, of the $2.57x of business interest expense that is ECI and that is attributable to interest expense on FC's share of liabilities of ABC (and its partnership interests), 50 percent ($250x of basis in the portion of the DEF partnership interest that would be a U.S. asset if ABC were a foreign corporation/ $500x total basis in assets that would be U.S. assets if ABC were a foreign corporation), or $1.29x, is attributable to interest expense on FC's share of liabilities of ABC and 50 percent ($250x of basis in assets other than partnership interests that would be U.S. assets if ABC were a foreign corporation/ $500x of total basis in assets that would be U.S. assets if ABC were a foreign corporation), or $1.29x is attributable to interest expense on FC's share of liabilities of DEF. As a result, $19.43x ($16x + $3.43x) of business interest expense is attributed to FC, $16.29x ($15x + $1.29x) of business interest expense is attributed to ABC, and $11.29x ($10x + $1.29x) of business interest expense is attributed to DEF. The limitation under paragraph (f)(1)(iii)(C)(*4*) of this section does not change the result described in the preceding sentence. Specifically, under paragraph (f)(1)(iii)(C)(*4*) of this section, the amount attributed to FC (tentatively, $3.43x) is limited to $19x (FC's business interest expense of $100x, reduced by $16x of business interest expense on U.S. booked liabilities of Business Y, its $40x allocable share of ABC's business interest expense, and its $25 allocable share of DEF's business interest expense); the amount attributed to ABC (tentatively, $1.29x) is limited to $25x (FC's 50-percent share of the $80x of business interest expense of ABC, or $40x, reduced by FC's 50-percent share of the $30x of business interest expense on U.S. booked liabilities of Business S, or $15x); and the amount attributed to DEF (tentatively, $1.29x) is limited to $15x (FC's 25-percent share of the $100x of business interest expense of DEF, or $25x, reduced by FC's 25-percent share of the $40x of business interest expense on U.S. booked liabilities of Business U, or $10x).

(C) *Application of section 163(j) to DEF*—(*1*) *In general.* Under § 1.163(j)–6(a), DEF computes a section 163(j) limitation at the partnership-level. DEF has business interest expense of $100x ($40x from Business U + $60x from Business V). Under § 1.163(j)–6(d), DEF has ATI of $240x ($100x + $140x). Under § 1.163(j)–2(b), DEF's section 163(j) limitation is $72x ($240x × 30 percent). Because DEF's business interest expense ($100x) exceeds the section 163(j) limitation ($72x), only $72x of DEF's business interest expense is deductible and $28x is disallowed under section 163(j). Pursuant to paragraph (e)(2) of this section, FC is allocated $7x of excess business interest expense (25 percent × $28x) and $18x of deductible business interest expense (25 percent × $72x).

(*2*) *Deductible business interest expense.* Under paragraph (c)(3) of this section, in order to determine the portion of FC's allocable deductible business interest expense ($18x) that is allocable ECI deductible BIE and the portion that is allocable non-ECI deductible BIE, the hypothetical partnership ECI deductible BIE and hypothetical partnership non-ECI deductible BIE must be determined. Under paragraph (c)(3)(iii)(A) of this section, FC's hypothetical partnership ECI deductible BIE with respect to DEF is $7.50x ($25x of FC's allocable share of ECI before taking into account interest expense × 30 percent). Under paragraph (c)(3)(iii)(B) of this section, FC's hypothetical partnership non-ECI deductible BIE with respect to DEF is $10.50x ($35x of FC's allocable share of income that is not ECI before taking into account interest expense × 30 percent). Under paragraph (c)(3)(i) of this section, allocable ECI deductible BIE is equal to the amounts described in paragraphs (c)(3)(ii)(A)(*1*)(*i*) and (c)(3)(ii)(B)(*1*) of this section and allocable non-ECI deductible BIE is equal to the amounts described in paragraphs (c)(3)(ii)(A)(*1*)(*ii*) and (c)(3)(ii)(B)(*2*) of this section. Under paragraph (c)(3)(ii)(A)(*1*) of this section, FC's allocable deductible business interest expense ($18x) is allocated pro rata between hypothetical partnership ECI deductible BIE ($7.50x) and hypothetical partnership non-ECI deductible BIE ($10.50x). However, the amount allocated to hypothetical partnership ECI deductible BIE cannot exceed the lesser of hypothetical partnership ECI deductible BIE ($7.50x) or allocable ECI BIE ($11.29x), and the amount allocated to hypothetical partnership non-ECI deductible BIE cannot exceed the lesser of hypothetical partnership non-ECI deductible BIE ($10.50x) or allocable non-ECI BIE (total allocable business interest expense of $25x reduced by allocable ECI BIE of $11.29x, or $13.71x). The portion of FC's allocable deductible business interest expense ($18x) from DEF that is allocable ECI deductible BIE is 41.67 percent ($7.50x of hypothetical partnership ECI deductible BIE/ $18x of total hypothetical partnership deductible BIE), or $7.5x. The portion of FC's allocable deductible business interest expense from DEF ($18x) that is allocable non-ECI deductible BIE is 58.33 percent ($10.50x of hypothetical partnership ECI deductible BIE/$18x of total hypothetical partnership deductible BIE), or $10.50x. Because the full amount of FC's allocable deductible business interest expense ($18x) is allocable under paragraph (c)(3)(ii)(A)(*1*) of this section, no portion is allocated under paragraph (c)(3)(ii)(B) of this section.

(*3*) *Excess business interest expense.* Under paragraph (c)(2)(i) of this section, the portion of excess business interest expense allocated to FC from DEF pursuant to paragraph (e)(2) of this section ($7x) that is allocable ECI excess BIE is $3.79x ($11.29x of allocable ECI BIE − $7.50x allocable ECI deductible BIE). Under paragraph (c)(2)(ii) of this section, the portion of excess business interest expense allocated to FC from DEF pursuant to paragraph (e)(2) of this section ($7x) that is allocable non-ECI excess BIE is $3.21x ($13.71x of allocable non-ECI BIE − $10.50x allocable non-ECI deductible BIE).

(D) *Application of section 163(j) to ABC*—(*1*) *In general.* Under § 1.163(j)–6(a), ABC computes a section 163(j) limitation at the partnership-level. ABC has business interest expense of $80x ($30x from Business S + $50x from Business T). Under § 1.163(j)–6(d), ABC has ATI of $170x ($80x + $90x). Under § 1.163(j)–2(b), ABC's section 163(j) limitation is $51x ($170x × 30 percent). Because ABC's business interest expense ($80x) exceeds the section 163(j) limitation ($51x), ABC may only deduct $51x of business interest expense, and $29x is disallowed under section 163(j). Pursuant to § 1.163(j)–6(f)(2), FC is allocated $14.50x of excess business interest expense (50 percent × $29x) and $25.50x of deductible business interest expense (50 percent × $51x).

(*2*) *Deductible business interest expense.* Under paragraph (c)(3) of this section, in order to determine the portion of FC's allocable deductible business interest expense ($25.50x) that is allocable ECI deductible BIE and the portion that is allocable non-ECI deductible BIE, the hypothetical partnership ECI deductible BIE and hypothetical partnership non-ECI deductible BIE must be determined. Under paragraph (c)(3)(iii)(A) of this section, FC's hypothetical partnership ECI deductible BIE with respect to ABC is $12x ($40x of FC's allocable share of ECI before taking into account interest expense × 30 percent). Under paragraph (c)(3)(iii)(B) of this section, FC's hypothetical partnership non-ECI deductible BIE with respect to ABC is $13.50x ($45x of FC's allocable share of income that is not ECI before taking into account interest expense × 30 percent). Under paragraph (c)(3)(i) of this section, allocable ECI deductible BIE is equal to the amounts described in paragraphs (c)(3)(ii)(A)(*1*)(*i*) and (c)(3)(ii)(B)(*1*) of this section and allocable non-ECI deductible BIE is equal to the amounts described in paragraphs (c)(3)(ii)(A)(*1*)(*ii*) and (c)(3)(ii)(B)(*2*) of this section. Under paragraph (c)(3)(ii)(A)(*1*) of this section, FC's allocable deductible business interest expense ($25.50x) is allocated pro rata between hypothetical partnership ECI deductible BIE ($12x) and hypothetical partnership non-ECI deductible BIE ($13.50x). However, the amount allocated to hypothetical partnership ECI deductible BIE cannot exceed the lesser of hypothetical partnership ECI deductible BIE ($12x) or allocable ECI BIE ($16.29x), and the amount allocated to hypothetical partnership non-ECI deductible BIE cannot exceed the lesser of hypothetical partnership non-ECI deductible BIE ($13.50x) or allocable non-ECI BIE (total allocable business interest expense of $40x reduced by allocable ECI BIE of $16.29x, or $23.71x). The portion of FC's allocable deductible business interest expense from ABC ($25.50x) that is allocable ECI deductible BIE is 47.06 percent ($12x of hypothetical partnership ECI deductible BIE/ $25.50x of total hypothetical partnership deductible BIE), or $12x. The portion of FC's allocable deductible business interest expense from ABC that is allocable non-ECI deductible BIE is 52.94 percent ($13.50x of hypothetical partnership ECI deductible BIE/ $25.50x of total hypothetical partnership deductible BIE), or $13.50x. Because the full amount of FC's allocable deductible business interest expense ($25.50x) is allocable under paragraph (c)(3)(ii)(A)(*1*) of this section, no portion is allocated under paragraph (c)(3)(ii)(B) of this section.

(*3*) *Excess business interest expense.* Under paragraph (c)(2)(i) of this section, the portion of excess business interest expense allocated to FC from ABC pursuant to § 1.163(j)–6(f)(2)($14.50x) that is allocable ECI excess BIE is $4.29x ($16.29x of allocable ECI BIE − $12x allocable ECI deductible BIE). Under paragraph (c)(2)(ii) of this section, the portion of excess business interest expense allocated to FC from ABC pursuant to § 1.163(j)–6(f)(2) ($14.50x) that is allocable non-ECI excess BIE is $10.21x ($23.71x of allocable non-ECI BIE − $13.50x allocable non-ECI deductible BIE).

(E) *Application of section 163(j) to FC.* Under paragraph (b)(3) of this section, FC's business interest expense is $19.43x. Under § 1.163(j)–6(e)(1), FC's ATI is determined under § 1.163(j)–1(b)(1) without regard to FC's distributive share of any items of income, gain, deduction, or loss of ABC or DEF. Under paragraph (b)(2) of this section, FC's ATI is $56x ($56x of ECI of Business Y before taking into account interest expense). FC's section 163(j) limitation is $16.80x ($56x × 30 percent). Because the portion of FC's business interest expense determined under § 1.882–5 that is attributed to FC ($19.43x) exceeds the section 163(j) limitation ($16.80x), FC may only deduction $16.80x of business interest expense, and $2.63x is disallowed business interest expense carryforward. After taking into account FC's allocable share of deductible business interest expense, FC may deduct $36.30x ($16.80x from FC + $12x allocable ECI deductible BIE from ABC + $7.50x allocable ECI deductible BIE from DEF). FC also has $2.63x disallowed business interest expense carryforward characterized as ECI, $4.29x allocable ECI excess BIE from ABC, $10.21x allocable non-ECI excess BIE from ABC, and, under paragraph (e)(2) of this section, is deemed to have $3.79x allocable ECI excess BIE from DEF and $3.21x allocable non-ECI excess BIE from DEF.

(i) [Reserved]

(j) *Applicability date.* This section applies to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply this section in its entirety for a taxable year beginning after December 31, 2017, so long as the taxpayers and their related parties also apply § 1.163(j)–7(a), (c) through (f), (g)(3) and (4), and (h) through (k) for the taxable year. For a taxable year beginning before November 13, 2020, taxpayers and their related parties may not choose to apply this section unless they also apply § 1.163(j)–7(b) and (g)(1) and (2) in accordance with the second sentence of § 1.163(j)–7(m)(1).

■ **Par. 10.** As added in a final rule elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.163(j)–10 is amended by:

■ 1. Designating paragraph (c)(5)(ii)(D) as paragraph (c)(5)(ii)(D)(*1*).

■ 2. Adding a subject heading for paragraph (c)(5)(ii)(D).

■ 3. Adding paragraph (c)(5)(ii)(D)(*2*).

■ 4. Designating paragraph (f) as paragraph (f)(1).

■ 5. Adding a subject heading for paragraph (f).

■ 6. Revising the subject heading of newly redesignated paragraph (f)(1).

■ 7. Adding paragraph (f)(2).

The additions and revision read as follows:

1.163(j)–10 Allocation of interest expense, interest income, and other items of expense and gross income to an excepted trade or business.

* * * * *

(c) * * *

(5) * * *

(ii) * * *

(D) *Limitations on application of look-through rules.* * * *

(*2*) *Limitation on application of look-through rule to C corporations.* Except as provided in § 1.163(j)–9(h)(4)(iii) and (iv) (for a REIT or a partnership making the election under § 1.163(j)–9(h)(1) or (7), respectively), for purposes of applying the look-through rules in paragraph (c)(5)(ii)(B) and (C) of this section to a non-consolidated C corporation (upper-tier entity), that upper-tier entity may not apply these look-through rules to a lower-tier non-consolidated C corporation. For example, assume that P wholly and directly owns S1 (the upper-tier entity), which wholly and directly owns S2. Further assume that each of these entities is a non-consolidated C corporation to which the small business exemption does not apply. S1 may not look through the stock of S2 (and may not apply the asset basis look-through rule described in paragraph (c)(5)(ii)(B)(*2*)(*iv*) of this section) for purposes of P's allocation of its basis in its S1 stock between excepted and non-excepted trades or businesses; instead, S1 must treat its stock in S2 as an asset used in a non-excepted trade or business for that purpose. However, S1 may look through the stock of S2 for purposes of S1's allocation of its basis in its S2 stock between excepted and non-excepted trades or businesses.

* * * * *

(f) *Applicability dates.*

(1) *In general.* * * *

(2) *Paragraph (c)(5)(ii)(D)(2).* The rules contained in paragraph (c)(5)(ii)(D)(*2*) of this section apply for taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers may choose to apply the rules of paragraph (c)(5)(ii)(D)(*2*) of this section to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], so long as they consistently apply the rules in the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.383–0, 1.383–1, 1.469–9, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4 to that taxable year and each subsequent taxable year.

■ **Par. 11.** Section 1.469–4 is amended by adding paragraph (d)(6) to read as follows:

§ 1.469–4 Definition of activity.

* * * * *

(d) * * *

(6) *Activities described in section 163(d)(5)(A)(ii).* An activity described in section 163(d)(5)(A)(ii) that involves the conduct of a trade or business which is not a passive activity of the taxpayer and with respect to which the taxpayer does not materially participate may not be grouped with any other activity or activities of the taxpayer, including any other activity described in section 163(d)(5)(A)(ii).

* * * * *

■ **Par. 12.** As amended in a final rule elsewhere in this issue of the **Federal Register**, effective November 13, 2020, § 1.469–9 is further amended by revising paragraphs (b)(2)(ii)(A) and (B) to read as follows:

§ 1.469–9 Rules for certain rental real estate activities.

* * * * *

(b) * * *

(2) * * *

(ii) * * *

(A) *Real property development.* The term *real property development* means the maintenance and improvement of raw land to make the land suitable for subdivision, further development, or construction of residential or commercial buildings, or to establish, cultivate, maintain or improve timberlands (that is, land covered by timber-producing forest). Improvement of land may include any clearing (such as through the mechanical separation and removal of boulders, rocks, brush, brushwood, and underbrush from the land); excavation and gradation work; diversion or redirection of creeks, streams, rivers, or other sources or bodies of water; and the installation of roads (including highways, streets, roads, public sidewalks, and bridges), utility lines, sewer and drainage systems, and any other infrastructure that may be necessary for subdivision, further development, or construction of residential or commercial buildings, or for the establishment, cultivation, maintenance or improvement of timberlands.

(B) *Real property redevelopment.* The term *real property redevelopment* means the demolition, deconstruction, separation, and removal of existing buildings, landscaping, and infrastructure on a parcel of land to return the land to a raw condition or otherwise prepare the land for new development or construction, or for the establishment and cultivation of new timberlands.

* * * * *

■ **Par. 13.** Section 1.469–11 is amended by revising paragraphs (a)(1) and (4) to read as follows:

§ 1.469–11 Applicability date and transition rules.

(a) * * *

(1) The rules contained in §§ 1.469–1, 1.469–1T, 1.469–2, 1.469–2T, 1.469–3, 1.469–3T, 1.469–4, but not § 1.469–4(d)(6), 1.469–5 and 1.469–5T apply for taxable years ending after May 10, 1992. The rules contained in § 1.469–4(d)(6) apply for taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b), may choose to apply the rules of § 1.469–4(d)(6) to a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], so long as they consistently apply the rules in the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.383–0, 1.383–1, 1.469–9, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4 to that taxable year and each subsequent taxable year.

* * * * *

(4) The rules contained in § 1.469–9(b)(2), other than paragraphs (b)(2)(ii)(A) and (B), apply to taxable years beginning on or after [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. Section 1.469–9(b)(2)(ii)(A) and (B) applies to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, within the meaning of sections 267(b) and 707(b)(1), may choose to apply the rules of § 1.469–9(b)(2), other than paragraphs (b)(2)(ii)(A) and (B), to a taxable year beginning after December 31, 2017, and before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**] and may choose to apply the rules contained in 1.469–9(b)(2)(ii)(A) and (B) to taxable years beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], so long as they consistently apply the rules of the section 163(j) regulations, and, if applicable, §§ 1.263A–9, 1.263A–15, 1.381(c)(20)–1, 1.382–1, 1.382–2, 1.382–5, 1.382–6, 1.383–0, 1.383–1, 1.469–9, 1.704–1, 1.882–5, 1.1362–3, 1.1368–1, 1.1377–1, 1.1502–13, 1.1502–21, 1.1502–79, 1.1502–91 through 1.1502–99 (to the extent they effectuate the rules of §§ 1.382–2, 1.382–5, 1.382–6, and 1.383–1), and 1.1504–4 to that taxable year and each subsequent taxable year.

* * * * *

■ **Par. 14.** Section 1.1256(e)–2 is added to read as follows:

§ 1.1256 (e)–2 Special rules for syndicates.

(a) *Allocation of losses.* For purposes of section 1256(e)(3), *syndicate* means any partnership or other entity (other than a corporation that is not an S corporation) if more than 35 percent of the losses of such entity during the taxable year are allocated to limited partners or limited entrepreneurs (within the meaning of section 461(k)(4)).

(b) *Determination of loss amount.* For purposes of section 1256(e)(3), the amount of losses to be allocated under paragraph (a) of this section is calculated without regard to section 163(j).

(c) *Example.* The following example illustrates the rules in this section:

(1) *Facts.* Entity is an S corporation that is equally owned by individuals A and B. A provides all of the goods and services provided by Entity. B provided all of the capital for Entity but does not participate in Entity's business. For the current taxable year, Entity has gross receipts of $5,000,000, non-interest expenses of $4,500,000, and interest expense of $600,000.

(2) *Analysis.* Under paragraph (b) of this section, Entity has a net loss of $100,000 ($5,000,000 minus $5,100,000) for the current taxable year. One half (50 percent) of this loss is allocated to B, a limited owner. Therefore, for the current taxable year, Entity is a syndicate within the meaning of section 1256(e)(3)(B).

(d) *Applicability date.* This section applies to taxable years beginning on or after [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**]. However, taxpayers and their related parties, under sections 267(b) and 707(b)(1), may choose to apply the rules of this section for a taxable year beginning after December 31, 2017, and before [DATE 60 DAYS AFTER DATE OF PUBLICATION OF THE FINAL RULE IN THE **FEDERAL REGISTER**], provided that they consistently apply the rules of this section to that taxable year and each subsequent taxable year.

Sunita Lough,

Deputy Commissioner for Services and Enforcement.

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Part III

Commodity Futures Trading Commission

17 CFR Part 23
Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants; Final Rule

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 23

RIN 3038–AE84

Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rule.

SUMMARY: The Commodity Futures Trading Commission (''Commission'' or ''CFTC'') is adopting a final rule (''Final Rule'') addressing the cross-border application of certain swap provisions of the Commodity Exchange Act (''CEA or ''Act''), as added by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (''Dodd-Frank Act''). The Final Rule addresses the cross-border application of the registration thresholds and certain requirements applicable to swap dealers (''SDs'') and major swap participants (''MSPs''), and establishes a formal process for requesting comparability determinations for such requirements from the Commission. The Final Rule adopts a risk-based approach that, consistent with the applicable section of the CEA, and with due consideration of international comity principles and the Commission's interest in focusing its authority on potential significant risks to the U.S. financial system, advances the goals of the Dodd-Frank Act's swap reforms, while fostering greater liquidity and competitive markets, promoting enhanced regulatory cooperation, and improving the global harmonization of swap regulation.

DATES: The Final Rule is effective November 13, 2020. Specific compliance dates are set forth in the Final Rule.

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I. Background

A. Statutory Authority and Prior Commission Action

In 2010, the Dodd-Frank Act [1] amended the CEA [2] to, among other things, establish a new regulatory framework for swaps. Added in the wake of the 2008 financial crisis, the Dodd-Frank Act was enacted to reduce systemic risk, increase transparency, and promote market integrity within the financial system. Given the global nature of the swap market, the Dodd-Frank Act amended the CEA by adding section 2(i) to provide that the swap provisions of the CEA enacted by Title VII of the Dodd-Frank Act (''Title VII''), including any rule prescribed or regulation promulgated under the CEA, shall not apply to activities outside the United States (''U.S.'') unless those activities have a direct and significant connection with activities in, or effect on, commerce of the United States, or they contravene Commission rules or regulations as are necessary or appropriate to prevent evasion of the swap provisions of the CEA enacted under Title VII.[3]

In May 2012, the CFTC and Securities and Exchange Commission (''SEC'') jointly issued an adopting release that, among other things, further defined and provided registration thresholds for SDs and MSPs in § 1.3 of the CFTC's regulations (''Entities Rule'').[4]

In July 2013, the Commission published interpretive guidance and a policy statement regarding the cross-border application of certain swap provisions of the CEA (''Guidance'').[5] The Guidance included the Commission's interpretation of the ''direct and significant'' prong of section 2(i) of the CEA.[6] In addition, the Guidance established a general, non-binding framework for the cross-border application of many substantive Dodd-Frank Act requirements, including registration and business conduct requirements for SDs and MSPs, as well as a process for making substituted compliance determinations. Given the complex and dynamic nature of the global swap market, the Guidance was intended to be a flexible and efficient way to provide the Commission's views on cross-border issues raised by market participants, allowing the Commission to adapt in response to changes in the global regulatory and market landscape.[7] The Commission accordingly stated that it would review and modify its cross-border policies as the global swap market continued to evolve and consider codifying the cross-border application of the Dodd-Frank Act swap provisions in future rulemakings, as appropriate.[8] At the time that it adopted the Guidance, the Commission was tasked with regulating a market that grew to a global scale without any meaningful regulation in the United States or overseas, and the United States was the first member country of the Group of 20 (''G20'') to adopt most of the swap reforms agreed to at the G20 Pittsburgh Summit in 2009.[9] Developing a regulatory framework to fit that market necessarily requires adapting and responding to changes in the global market, including developments resulting from requirements imposed on market participants under the Dodd-Frank Act and the Commission's implementing regulations in the U.S., as well as those that have been imposed by non-U.S. regulatory authorities since the Guidance was issued.

On November 14, 2013, DSIO issued a staff advisory (''ANE Staff Advisory'') stating that a non-U.S. SD that regularly uses personnel or agents located in the United States to arrange, negotiate, or execute a swap with a non-U.S. person (''ANE Transactions'') would generally be required to comply with ''Transaction-Level Requirements,'' as the term was used in the Guidance (discussed in section V.A).[10] On November 26, 2013, Commission staff issued certain no-action relief to non-U.S. SDs registered with the Commission from these requirements in connection with ANE Transactions (''ANE No-Action Relief'').[11] In January 2014, the Commission published a request for comment on all aspects of the ANE Staff Advisory (''ANE Request for Comment'').[12]

In May 2016, the Commission issued a final rule on the cross-border application of the Commission's margin requirements for uncleared swaps (''Cross-Border Margin Rule'').[13] Among other things, the Cross-Border Margin Rule addressed the availability of substituted compliance by outlining the circumstances under which certain SDs and MSPs could satisfy the Commission's margin requirements for uncleared swaps by complying with comparable foreign margin requirements. The Cross-Border Margin Rule also established a framework by which the Commission assesses whether a foreign jurisdiction's margin requirements are comparable.

In October 2016, the Commission proposed regulations regarding the cross-border application of certain requirements under the Dodd-Frank Act regulatory framework for SDs and MSPs (''2016 Proposal'').[14] The 2016 Proposal incorporated various aspects of the Cross-Border Margin Rule and addressed when U.S. and non-U.S. persons, such as foreign consolidated subsidiaries (''FCSs'') and non-U.S. persons whose swap obligations are guaranteed by a U.S. person, would be required to include swaps or swap positions in their SD or MSP registration threshold calculations, respectively.[15] The 2016 Proposal also addressed the extent to which SDs and MSPs would be required to comply with the Commission's business conduct standards governing their conduct with swap counterparties (''external business conduct standards'') in cross-border

[1] Public Law 111–203, 124 Stat. 1376 (2010).

[2] 7 U.S.C. 1 *et seq.*

[3] 7 U.S.C. 2(i).

[4] *See* 17 CFR 1.3; ''Swap dealer'' and ''Major swap participant''; Further Definition of ''Swap Dealer,'' ''Security-Based Swap Dealer,'' ''Major Swap Participant,'' ''Major Security-Based Swap Participant'' and ''Eligible Contract Participant,'' 77 FR 30596 (May 23, 2012). Commission regulations referred to herein are found at 17 CFR chapter I.

[5] *See* Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 FR 45292 (Jul. 26, 2013).

[6] *Id.* at 45297–45301. The Commission is now restating this interpretation, as discussed in section I.D.2 *infra.*

[7] *Id.* at 45297 n.39.

[8] *See id.*

[9] *See* G20 Leaders' Statement: The Pittsburgh Summit, A Framework for Strong, Sustainable, and Balanced Growth (Sep. 24–25, 2009), available at *https://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf.*

[10] *See* CFTC Staff Advisory No. 13–69, Applicability of Transaction-Level Requirements to Activity in the United States (Nov. 14, 2013), available at *http://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/13-69.pdf.* All Commission staff letters are available at *https://www.cftc.gov/LawRegulation/CFTCStaffLetters/index.htm.*

[11] CFTC Staff Letter No. 13–71, No-Action Relief: Certain Transaction-Level Requirements for Non-U.S. Swap Dealers (Nov. 26, 2013), available at *https://www.cftc.gov/csl/13-71/download.* Commission staff subsequently extended this relief in CFTC Letter Nos. 14–01, 14–74, 14–140, 15–48, 16–64, and 17–36.

[12] Request for Comment on Application of Commission Regulations to Swaps Between Non-U.S. Swap Dealers and Non-U.S. Counterparties Involving Personnel or Agents of the Non-U.S. Swap Dealers Located in the United States, 79 FR 1347, 1348–49 (Jan. 8, 2014).

[13] Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants—Cross-Border Application of the Margin Requirements, 81 FR 34818 (May 31, 2016).

[14] Cross-Border Application of the Registration Thresholds and External Business Conduct Standards Applicable to Swap Dealers and Major Swap Participants, 81 FR 71946 (proposed Oct. 18, 2016).

[15] *Id.* at 71947. As noted above, the SD and MSP registration thresholds are codified in the definitions of those terms at 17 CFR 1.3.

transactions.[16] In addition, the 2016 Proposal addressed ANE Transactions, including the types of activities that would constitute arranging, negotiating, and executing within the context of the 2016 Proposal, the treatment of such transactions with respect to the SD registration threshold, and the application of external business conduct standards with respect to such transactions.[17]

B. Proposed Rule and Brief Summary of Comments Received

In January 2020, the Commission published a notice of proposed rulemaking (''Proposed Rule''), which proposed to: (1) Address the cross-border application of the registration thresholds and certain requirements applicable to SDs and MSPs; and (2) establish a formal process for requesting comparability determinations for such requirements from the Commission.[18] In the Proposed Rule, the Commission also withdrew the 2016 Proposal, stating that the Proposed Rule reflected the Commission's current views on the matters addressed in the 2016 Proposal, which had evolved since the 2016 Proposal as a result of market and regulatory developments in the swap markets and in the interest of international comity.[19] The Commission requested comments generally on all aspects of the Proposed Rule and on many specific questions.

The Commission received 18 relevant comment letters.[20] Though AFR and IATP did not support the Commission adopting the Proposed Rule in its entirety, most commenters were supportive of the Proposed Rule, generally, or supportive of specific elements of the Proposed Rule. However, many of these commenters suggested modifications to portions of the Proposed Rule, which are discussed in the relevant sections discussing the Final Rule below. In addition, several commenters requested Commission action beyond the scope of the Proposed Rule.[21] Further, IIB/SIFMA requested that the Commission re-visit in the Final Rule the applicability of the Commission's cross-border uncleared swap margin requirements that were addressed in the Cross-Border Margin Rule. The Commission addressed those requirements in the Cross-Border Margin Rule, did not propose modifying them in the Proposed Rule, and therefore is not making any changes to the Cross-Border Margin Rule in this Final Rule.

C. Global Regulatory and Market Structure

As noted in the Proposed Rule, the regulatory landscape is far different now than it was when the Dodd-Frank Act was enacted in 2010.[22] When the CFTC published the Guidance in 2013, very few jurisdictions had made significant progress in implementing the global swap reforms to which the G20 leaders agreed at the Pittsburgh G20 Summit. Today, however, as a result of the cumulative implementation efforts by regulators throughout the world, significant progress has been made in the world's primary swap trading jurisdictions to implement the G20 commitments.[23] Since the enactment of the Dodd-Frank Act, regulators in a number of large developed markets have adopted regulatory regimes that are designed to mitigate systemic risks associated with a global swap market. These regimes include central clearing requirements, margin requirements for non-centrally cleared derivatives, and other risk mitigation requirements.[24]

Many swaps involve at least one counterparty that is located in the United States or another jurisdiction that has adopted comprehensive swap regulations.[25] Conflicting and duplicative requirements between U.S. and foreign regimes can contribute to potential market inefficiencies and regulatory arbitrage, as well as competitive disparities that undermine the relative positions of U.S. SDs and their counterparties. This may result in market fragmentation, which can lead to significant inefficiencies that result in additional costs to end-users and other market participants. Market fragmentation can also reduce the capacity of financial firms to serve both domestic and international customers.[26] The Final Rule supports a cross-border framework that promotes the integrity, resilience, and vibrancy of the swap market while furthering the important policy goals of the Dodd-Frank Act. In that regard, it is important to consider how market practices have evolved since the publication of the Guidance. As certain market participants may have conformed their practices to the Guidance, the Final Rule will ideally cause limited additional costs and burdens for these market participants, while supporting the continued operation of markets that are much more comprehensively regulated than they were before the Dodd-Frank Act and the actions of governments worldwide taken in response to the Pittsburgh G20 Summit.

The approach described below is informed by the Commission's understanding of current market practices of global financial institutions under the Guidance. For business and regulatory reasons, a financial group that is active in the swap market often operates in multiple market centers around the world and carries out swap activity with geographically-diverse counterparties using a number of different operational structures.[27]

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[16] *Id.* The Commission's external business conduct standards are codified in 17 CFR part 23, subpart H (17 CFR 23.400 through 23.451).

[17] 2016 Proposal, 81 FR at 71947.

[18] Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants, 85 FR 952 (proposed Jan. 8, 2020).

[19] *Id.* at 954.

[20] The Commission received comments from Alternative Investment Management Association (''AIMA''); Americans for Financial Reform Education Fund (''AFR''); Associated Foreign Exchange, Inc. & GPS Capital Markets, Inc. (''AFEX/GPS''); Chris Barnard (''Barnard''); Better Markets, Inc. (''Better Markets''); BGC Partners & Tradition America Holdings, Inc. (''BGC/Tradition''); Chatham Financial (''Chatham''); Citadel (''Citadel''); Commercial Energy Working Group (''Working Group''); Credit Suisse (''CS''); Futures Industry Association (''FIA''); Japan Financial Markets Council & International Bankers Association of Japan (''JFMC/IBAJ''); Institute for Agriculture and Trade Policy (''IATP''); Institute of International Bankers & Securities Industry and Financial Markets Association (''IIB/SIFMA''); International Swaps and Derivatives Association (''ISDA''); Japanese Bankers Association (''JBA''); Japan Securities Clearing Corporation (''JSCC''); and State Street Corporation (''State Street''). The Commission also received letters from PT Arba Sinar Jaya, Robert Ware (UIUC), and William Harrington that were not relevant to the Proposed Rule. All comments on the Proposed Rule are available at *https://comments.cftc.gov/PublicComments/CommentList.aspx?id=3067.*

[21] *See infra* section VIII for a discussion of these comments.

[22] Proposed Rule, 85 FR at 954–955.

[23] *See, e.g.,* Financial Stability Board (''FSB''), OTC Derivatives Market Reforms: 2019 Progress Report on Implementation (Oct. 15, 2019) (''2019 FSB Progress Report''), available at *https://www.fsb.org/wp-content/uploads/P151019.pdf;* FSB, Implementation and Effects of the G20 Financial Regulatory Reforms: Fourth Annual Report (Nov. 28, 2018), available at *http://www.fsb.org/wp-content/uploads/P281118-1.pdf.*

[24] For example, at the end of September 2019, 16 FSB member jurisdictions had comprehensive swap margin requirements in force. *See* 2019 FSB Progress Report, at 2.

[25] *See, e.g.,* 2019 FSB Progress Report; Bank of International Settlements (''BIS''), Triennial Central Bank Survey of Foreign Exchange and Over-the-counter Derivatives Markets in 2019 (Sep. 16, 2019), available at *https://www.bis.org/statistics/rpfx19.htm.*

[26] *See, e.g.,* Institute of International Finance, Addressing Market Fragmentation: The Need for Enhanced Global Regulatory Cooperation (Jan. 2019), available at *https://www.iif.com/Portals/0/Files/IIF%20FSB%20Fragmentation%20Report.pdf.*

[27] *See* BIS, Committee on the Global Financial System, No. 46, The macrofinancial implications of alternative configurations for access to central counterparties in OTC derivatives markets, at 1 (Nov. 2011), available at *http://www.bis.org/publ/cgfs46.pdf* (stating that ''[t]he configuration of access must take account of the globalised nature of the market, in which a significant proportion of OTC derivatives trading is undertaken across borders'').

Financial groups often prefer to operate their swap dealing businesses and manage their swap portfolios in the jurisdiction where the swaps and the underlying assets have the deepest and most liquid markets. In operating their swap dealing businesses in these market centers, financial groups seek to take advantage of expertise in products traded in those centers and obtain access to greater liquidity. These arrangements permit them to price products more efficiently and compete more effectively in the global swap market, including in jurisdictions different from the market center in which the swap is traded.

In this sense, a global financial enterprise effectively operates as a single business, with a highly integrated network of business lines and services conducted through various branches or affiliated legal entities that are under the control of the parent entity.[28] Branches and affiliates in a global financial enterprise are highly interdependent, with separate entities in the group providing financial or credit support to each other, such as in the form of a guarantee or the ability to transfer risk through inter-affiliate trades or other offsetting transactions. Even in the absence of an explicit arrangement or guarantee, a parent entity may, for reputational or other reasons, choose to assume the risk incurred by its affiliates located overseas. Swaps are also traded by an entity in one jurisdiction, but booked and risk-managed by an affiliate in another jurisdiction. The Final Rule recognizes that these and similar arrangements among global financial enterprises create channels through which swap-related risks can have a direct and significant connection with activities in, or effect on, commerce of the United States.

D. Interpretation of CEA Section 2(i)

1. Proposed Rule and Discussion of Comments

The Proposed Rule set forth the Commission's interpretation of CEA section 2(i), which mirrored the approach that the Commission took in the Guidance.

Several commenters provided their views on the Commission's interpretation of CEA section 2(i). Better Markets agreed with the Commission's description of the Commission's authority to regulate swaps activities outside of the United States, recognizing that CEA section 2(i)'s mandatory exclusion of only certain, limited non-U.S. activities (*i.e.,* those that do not have a direct and significant connection with activities in, or effect on, U.S. commerce) evidences clear congressional intent to preserve jurisdiction with respect to others. Better Markets stated its belief that this reflects an intent to ensure U.S. law broadly applies to non-U.S. activities having requisite U.S. connections or effects. Better Markets argued, however, that the Commission does not have the discretion to determine whether and when to apply U.S. regulatory requirements based on vague principles of international comity, stating that the Commission has not cited a legally valid basis for its repeated reliance on international comity, where it simultaneously acknowledges direct and significant risks to the U.S. financial system.

BGC/Tradition supported the Commission's analysis related to CEA section 2(i) and what constitutes ''direct and significant.'' Specifically, BGC/Tradition agreed that the appropriate approach is ''to apply the swap provisions of the CEA to activities outside the United States that have either: (1) A direct and significant effect on U.S. commerce; or, in the alternative, (2) a direct and significant connection with activities in U.S. commerce, and through such connection present the type of risks to the U.S. financial system and markets that Title VII directed the Commission to address.''

IIB/SIFMA discussed the Commission's interpretation of ''direct'' in CEA section 2(i) and argued that the Commission should have followed Supreme Court precedent interpreting the ''direct effect'' test found in the Foreign Sovereign Immunities Act of 1976, which the Court has interpreted to be satisfied only by conduct abroad that has ''an immediate consequence'' in the United States.[29] IIB/SIFMA argued that a case cited by the Commission as a factor in its interpretation, the Seventh Circuit *en banc* decision in *Minn-Chem, Inc.* v. *Agrium, Inc.,* was based on considerations that are relevant to the Foreign Trade Antitrust Improvements Act of 1982 (''FTAIA''),[30]—but *not* section 2(i)—namely that (a) because the FTAIA includes the word ''foreseeable'' along with ''direct,'' the word ''direct'' should be interpreted as part of an integrated phrase that includes ''foreseeable'' effects, and (b) the FTAIA already addresses foreign conduct that has an immediate consequence in the United States through its separate provision for import commerce.[31] But, IIB/SIFMA argued, CEA section 2(i) does not include the word ''foreseeable,'' nor does it include any other provisions addressing foreign conduct that have an immediate consequence within the United States, so the *Minn-Chem* Court's reasoning does not support the Commission's decision to discount the Supreme Court's interpretation of the word ''direct'' in *Weltover.*

IATP argued that the Commission did not provide a sufficient ''international comity'' argument to justify deviating from the plain meaning of ''direct,'' nor a sufficient argument to rely on FTAIA case law to interpret ''direct.'' IATP stated its belief that the Commission's reliance on cross-border anti-trust trade law to interpret its statutory authority under CEA section 2(i) is an inconsistent and unreliable foundation for a rule that proposes no measures to prevent or discipline SDs' unreasonable restraint of trade. IATP recommended that the Commission abandon its ''restatement'' of its CEA section 2(i) authority and rely on a plain reading of CEA section 2(i).

In response to Better Markets' contention that the Commission does not have the discretion to determine whether and when to apply U.S. regulatory requirements based on principles of international comity where it simultaneously acknowledges direct and significant risks to the U.S. financial system, the Commission has followed the Restatement of Foreign Relations law in striving to minimize conflicts with the laws of other jurisdictions while seeking, pursuant to CEA section 2(i), to apply the swaps requirements of Title VII to activities outside the United States that have a direct and significant connection with activities in, or effect on, U.S. commerce. The Commission has determined that the rule appropriately accounts for these competing interests, ensuring that the Commission can discharge its responsibilities to protect the U.S. markets, market participants, and financial system, consistent with international comity, as set forth in the Restatement.

With respect to IIB/SIFMA's contention that the Commission erred in its interpretation of the meaning of ''direct'' in CEA section 2(i), IIB/SIFMA incorrectly asserted that the

[28] The largest U.S. banks have thousands of affiliated global entities, as shown in data from the National Information Center (''NIC''), a repository of financial data and institutional characteristics of banks and other institutions for which the Federal Reserve Board has a supervisory, regulatory, or research interest. *See* NIC, available at *https://www.ffiec.gov/npw.*

[29] *See Republic of Argentina* v. *Weltover,* 504 U.S. 607, 618 (1992).

[30] 15 U.S.C. 6a.

[31] *See Minn-Chem, Inc.* v. *Agrium, Inc.,* 683 F.3d 845, 857 (7th Cir. 2012).

Commission relied on the Seventh Circuit *en banc* decision in *Minn-Chem, Inc.* v. *Agrium, Inc.* Rather, the Commission was clear that its interpretation of CEA section 2(i) is not reliant on the reasoning of any individual judicial decision, but instead is drawn from a holistic understanding of both the statutory text *and* legal analysis applied by courts to analogous statutes and circumstances, specifically noting that the Commission's interpretation of CEA section 2(i) is not solely dependent on one's view of the Seventh Circuit's *Minn-Chem* decision,[32] but informed by its overall understanding of the relevant legal principles.

Finally, the Commission disagrees with IATP's advice that the Commission should abandon its interpretation of CEA section 2(i) and proceed with a ''plain reading'' of the statute. The Commission believes that IATP's assertion that the extraterritorial provisions of FTAIA and the case law construing such provisions are not relevant to CEA section 2(i) because the rule is not concerned with the regulation of anti-competitive behavior misconstrues the use that the Commission's interpretation has made of the Federal case law construing the meaning of the word ''direct'' in CEA section 2(i).[33]

2. Final Interpretation

In light of the foregoing, the Commission is restating its interpretation of section 2(i) of the CEA with its adoption of the Final Rule in substantially the same form as appeared in the Proposed Rule.

CEA section 2(i) provides that the swap provisions of Title VII shall not apply to activities outside the United States unless those activities—

- Have a direct and significant connection with activities in, or effect on, commerce of the United States; or
- Contravene such rules or regulations as the Commission may prescribe or promulgate as are necessary or appropriate to prevent the evasion of any provision of the CEA that was enacted by the Dodd-Frank Act.

The Commission believes that section 2(i) provides it express authority over swap activities outside the United States when certain conditions are met, but it does not require the Commission to extend its reach to the outer bounds of that authorization. Rather, in exercising its authority with respect to swap activities outside the United States, the Commission will be guided by international comity principles and will focus its authority on potential significant risks to the U.S. financial system.

(i) Statutory Analysis

In interpreting the phrase ''direct and significant,'' the Commission has examined the plain language of the statutory provision, similar language in other statutes with cross-border application, and the legislative history of section 2(i).

The statutory language in CEA section 2(i) is structured similarly to the statutory language in the FTAIA,[34] which provides the standard for the cross-border application of the Sherman Antitrust Act (''Sherman Act'').[35] The FTAIA, like CEA section 2(i), excludes certain non-U.S. commercial transactions from the reach of U.S. law. Specifically, the FTAIA provides that the antitrust provisions of the Sherman Act shall not apply to anti-competitive conduct involving trade or commerce with foreign nations.[36] However, like paragraph (1) of CEA section 2(i), the FTAIA also creates exceptions to the general exclusionary rule and thus brings back within antitrust coverage any conduct that: (1) Has a direct, substantial, and reasonably foreseeable effect on U.S. commerce; [37] and (2) such effect gives rise to a Sherman Act claim.[38] In *F. Hoffman-LaRoche, Ltd.* v. *Empagran S.A.,* the U.S. Supreme Court stated that ''this technical language initially lays down a general rule placing *all* (nonimport) activity involving foreign commerce outside the Sherman Act's reach. It then brings such conduct back within the Sherman Act's reach *provided that* the conduct *both* (1) sufficiently affects American commerce, *i.e.,* it has a 'direct, substantial, and reasonably foreseeable effect' on American domestic, import, or (certain) export commerce, *and* (2) has an effect of a kind that antitrust law considers harmful, *i.e.,* the 'effect' must 'giv[e] rise to a [Sherman Act] claim.' '' [39]

It is appropriate, therefore, to read section 2(i) of the CEA as a clear expression of congressional intent that the swap provisions of Title VII of the Dodd-Frank Act apply to activities beyond the borders of the United States when certain circumstances are present.[40] These circumstances include, pursuant to paragraph (1) of section 2(i), when activities outside the United States meet the statutory test of having a ''direct and significant connection with activities in, or effect on,'' U.S. commerce.

An examination of the language in the FTAIA, however, does not provide an unambiguous roadmap for the Commission in interpreting section 2(i) of the CEA because there are both similarities, and a number of significant differences, between the language in CEA section 2(i) and the language in the FTAIA. Further, the Supreme Court has not provided definitive guidance as to the meaning of the direct, substantial, and reasonably foreseeable test in the FTAIA, and the lower courts have interpreted the individual terms in the FTAIA differently.

Although a number of courts have interpreted the various terms in the FTAIA, only the term ''direct'' appears in both CEA section 2(i) and the FTAIA.[41] Relying upon the Supreme Court's definition of the term ''direct'' in the Foreign Sovereign Immunities Act (''FSIA''),[42] the U.S. Court of Appeals for the Ninth Circuit construed the term ''direct'' in the FTAIA as requiring a ''relationship of logical causation,'' [43] such that ''an effect is 'direct' if it follows as an immediate consequence of the defendant's activity.'' [44] However, in an *en banc* decision, *Minn-Chem, Inc.* v. *Agrium, Inc.,* the U.S. Court of Appeals for the Seventh Circuit held that ''the Ninth Circuit jumped too quickly on the assumption that the FSIA and the FTAIA use the word 'direct' in the same way.'' [45] After examining the text of the FTAIA as well as its history and

[32] *See* Proposed Rule, 85 FR at 956.

[33] *See infra* notes 41–51, and accompanying text.

[34] 15 U.S.C. 6a.

[35] 15 U.S.C. 1–7.

[36] 15 U.S.C. 6a.

[37] 15 U.S.C. 6a(1).

[38] 15 U.S.C. 6a(2).

[39] 542 U.S. 155, 162 (2004) (emphasis in original).

[40] *SIFMA* v. *CFTC,* 67 F.Supp.3d 373, 425–26 (D.D.C. 2014) (''The plain text of this provision 'clearly expresse[s]' Congress's 'affirmative intention' to give extraterritorial effect to Title VII's statutory requirements, as well as to the Title VII rules or regulations prescribed by the CFTC, whenever the provision's jurisdictional nexus is satisfied.''). *See also Prime Int'l Trading, Ltd.* v. *BP P.L.C.,* 937 F.3d 94, 103 (2d Cir. 2019) (stating that ''Section 2(i) contains, on its face, a 'clear statement,' *Morrison,* 561 U.S. at 265, 130 S.Ct. 2869, of extraterritorial application'' and describing it as ''an enumerated extraterritorial command'').

[41] Guidance, 78 FR at 45299.

[42] *See* 28 U.S.C. 1605(a)(2).

[43] *United States* v. *LSL Biotechnologies,* 379 F.3d 672, 693 (9th Cir. 2004). ''As a threshold matter, many courts have debated whether the FTAIA established a new jurisdictional standard or merely codified the standard applied in [*United States* v. *Aluminum Co. of Am.,* 148 F.2d 416 (2d Cir. 1945)] and its progeny. Several courts have raised this question without answering it. The Supreme Court did as much in [*Harford Fire Ins. Co.* v. *California,* 509 U.S. 764 (1993)].'' *Id.* at 678.

[44] *Id.* at 692–93, *quoting Republic of Argentina* v. *Weltover, Inc.,* 504 U.S. 607, 618 (1992) (providing that, pursuant to the FSIA, 28 U.S.C. 1605(a)(2), immunity does not extend to commercial conduct outside the United States that ''causes a direct effect in the United States'').

[45] *Minn-Chem, Inc.* v. *Agrium, Inc.,* 683 F.3d 845, 857 (7th Cir. 2012) (*en banc*).

purpose, the Seventh Circuit found persuasive the ''other school of thought [that] has been articulated by the Department of Justice's Antitrust Division, which takes the position that, for FTAIA purposes, the term 'direct' means only 'a reasonably proximate causal nexus.' '' [46] The Seventh Circuit rejected interpretations of the term ''direct'' that included any requirement that the consequences be foreseeable, substantial, or immediate.[47] In 2014, the U.S. Court of Appeals for the Second Circuit followed the reasoning of the Seventh Circuit in the *Minn-Chem* decision.[48] That said, the Commission would like to make clear that its interpretation of CEA section 2(i) is not reliant on the reasoning of any individual judicial decision, but instead is drawn from a holistic understanding of both the statutory text *and* legal analysis applied by courts to analogous statutes and circumstances. In short, as the discussion below will illustrate, the Commission's interpretation of section 2(i) is not solely dependent on one's view of the Seventh Circuit's *Minn-Chem* decision, but informed by its overall understanding of the relevant legal principles.

Other terms in the FTAIA differ from the terms used in section 2(i) of the CEA. First, the FTAIA test explicitly requires that the effect on U.S. commerce be a ''reasonably foreseeable'' result of the conduct,[49] whereas section 2(i) of the CEA, by contrast, does not provide that the effect on U.S. commerce must be foreseeable. Second, whereas the FTAIA solely relies on the ''effects'' on U.S. commerce to determine cross-border application of the Sherman Act, section 2(i) of the CEA refers to both ''effect'' and ''connection.'' ''The FTAIA says that the Sherman Act applies to foreign 'conduct' with a certain kind of harmful domestic effect.'' [50] Section 2(i), by contrast, applies more broadly—not only to particular instances of conduct that have an effect on U.S. commerce, but also to activities that have a direct and significant ''connection with activities in'' U.S. commerce. Unlike the FTAIA, section 2(i) applies the swap provisions of the CEA to activities outside the United States that have the requisite connection with activities in U.S. commerce, regardless of whether a ''harmful domestic effect'' has occurred.

As the foregoing textual analysis of the relevant statutory language indicates, section 2(i) differs from its analogue in the antitrust laws. Congress delineated the cross-border scope of the Sherman Act in section 6a of the FTAIA as applying to conduct that has a ''direct,'' ''substantial,'' and ''reasonably foreseeable'' ''effect'' on U.S. commerce. In section 2(i), on the other hand, Congress did not include a requirement that the effects or connections of the activities outside the United States be ''reasonably foreseeable'' for the Dodd-Frank Act swap provisions to apply. Further, Congress included language in section 2(i) to apply the Dodd-Frank Act swap provisions in circumstances in which there is a direct and significant connection with activities in U.S. commerce, regardless of whether there is an effect on U.S. commerce. The different words that Congress used in paragraph (1) of section 2(i), as compared to its closest statutory analogue in section 6a of the FTAIA, inform the Commission in construing the boundaries of its cross-border authority over swap activities under the CEA.[51] Accordingly, the Commission believes it is appropriate to interpret section 2(i) such that it applies to activities outside the United States in circumstances in addition to those that would be reached under the FTAIA standard.

One of the principal rationales for the Dodd-Frank Act was the need for a comprehensive scheme of systemic risk regulation. More particularly, a primary purpose of Title VII of the Dodd-Frank Act is to address risk to the U.S. financial system created by interconnections in the swap market.[52] Title VII of the Dodd-Frank Act gave the Commission new and broad authority to regulate the swap market to address and mitigate risks arising from swap activities that could adversely affect the resiliency of the financial system in the future.

In global markets, the source of such risk is not confined to activities within U.S. borders. Due to the interconnectedness between firms, traders, and markets in the U.S. and abroad, a firm's failure, or trading losses overseas, can quickly spill over to the United States and affect activities in U.S. commerce and the stability of the U.S. financial system. Accordingly, Congress explicitly provided for cross-border application of Title VII to activities outside the United States that pose risks to the U.S. financial system.[53] Therefore, the Commission construes section 2(i) to apply the swap provisions of the CEA to activities outside the United States that have either: (1) A direct and significant effect on U.S. commerce; or, in the alternative, (2) a direct and significant connection with activities in U.S. commerce, and through such connection present the

[46] *Id.*

[47] *Id.* at 856–57.

[48] *Lotes Co., Ltd.* v. *Hon Hai Precision Industry Co.,* 753 F.3d 395, 406–08 (2d Cir. 2014).

[49] *See, e.g., Animal Sciences Products.* v. *China Minmetals Corp.,* 654 F.3d 462, 471 (3d Cir. 2011) (''[T]he FTAIA's 'reasonably foreseeable' language imposes an objective standard: the requisite 'direct' and 'substantial' effect must have been 'foreseeable' to an objectively reasonable person.'').

[50] *Hoffman-LaRoche,* 452 U.S. at 173.

[51] The provision that ultimately became section 722(d) of the Dodd-Frank Act was added during consideration of the legislation in the House of Representatives. *See* 155 Cong. Rec. H14685 (Dec. 10, 2009). The version of what became Title VII that was reported by the House Agriculture Committee and the House Financial Services Committee did not include any provision addressing cross-border application. *See* 155 Cong. Rec. H14549 (Dec. 10, 2009). The Commission finds it significant that, in adding the cross-border provision before final passage, the House did so in terms that, as discussed in text, were different from, and broader than, the terms used in the analogous provision of the FTAIA.

[52] *Cf.* 156 Cong. Rec. S5818 (July 14, 2010) (statement of Sen. Lincoln) (''In 2008, our Nation's economy was on the brink of collapse. America was being held captive by a financial system that was so interconnected, so large, and so irresponsible that our economy and our way of life were about to be destroyed.''), available at *http://www.gpo.gov/fdsys/pkg/CREC-2010-07-14/pdf/CREC-2010-07-14.pdf;* 156 Cong. Rec. S5888 (July 15, 2010) (statement of Sen. Shaheen) (''We need to put in place reforms to stop Wall Street firms from growing so big and so interconnected that they can threaten our entire economy.''), available at *http://www.gpo.gov/fdsys/pkg/CREC-2010-07-15/pdf/CREC-2010-07-15-senate.pdf;* 156 Cong. Rec. S5905 (July 15, 2010) (statement of Sen. Stabenow) (''For too long the over-the-counter derivatives market has been unregulated, transferring risk between firms and creating a web of fragility in a system where entities became too interconnected to fail.''), available at *http://www.gpo.gov/fdsys/pkg/CREC-2010-07-15/pdf/CREC-2010-07-15-senate.pdf.*

[53] The legislative history of the Dodd-Frank Act shows that in the fall of 2009, neither the Over-the-Counter Derivatives Markets Act of 2009, H.R. 3795, 111th Cong. (1st Sess. 2009), reported by the Financial Services Committee chaired by Rep. Barney Frank, nor the Derivatives Markets Transparency and Accountability Act of 2009, H.R. 977, 111th Cong. (1st Sess. 2009), reported by the Agriculture Committee chaired by Rep. Collin Peterson, included a general territoriality limitation that would have restricted Commission regulation of transactions between two foreign persons located outside of the United States. During the House Financial Services Committee markup on October 14, 2009, Rep. Spencer Bachus offered an amendment that would have restricted the jurisdiction of the Commission over swaps between non-U.S. resident persons transacted without the use of the mails or any other means or instrumentality of interstate commerce. Chairman Frank opposed the amendment, noting that there may well be cases where non-U.S. residents are engaging in transactions that have an effect on the United States and that are insufficiently regulated internationally and that he would not want to prevent U.S. regulators from stepping in. Chairman Frank expressed his commitment to work with Rep. Bachus going forward, and Rep. Bachus withdrew the amendment. *See* H. Fin. Serv. Comm. Mark Up on Discussion Draft of the Over-the-Counter Derivatives Markets Act of 2009, 111th Cong., 1st Sess. (Oct. 14, 2009) (statements of Rep. Bachus and Rep. Frank), available at *http://financialservices.house.gov/calendar/eventsingle.aspx?EventID=231922.*

type of risks to the U.S. financial system and markets that Title VII directed the Commission to address. The Commission interprets section 2(i) in a manner consistent with the overall goal of the Dodd-Frank Act to reduce risks to the resiliency and integrity of the U.S. financial system arising from swap market activities.[54] Consistent with this interpretation, the Commission interprets the term ''direct'' in section 2(i) to require a reasonably proximate causal nexus, and not to require foreseeability, substantiality, or immediacy.

Further, the Commission does not interpret section 2(i) to require a transaction-by-transaction determination that a specific swap outside the United States has a direct and significant connection with activities in, or effect on, commerce of the United States to apply the swap provisions of the CEA to such transaction. Rather, it is the connection of swap activities, viewed as a class or in the aggregate, to activities in commerce of the United States that must be assessed to determine whether application of the CEA swap provisions is warranted.[55]

Similar interpretations of other federal statutes regulating interstate commerce support the Commission's interpretation here. For example, the Supreme Court has long supported a similar ''aggregate effects'' approach when analyzing the reach of U.S. authority under the Commerce Clause.[56] The Court phrased the holding in the seminal ''aggregate effects'' decision, *Wickard* v. *Filburn,*[57] in this way: ''[The farmer's] decision, when considered in the aggregate along with similar decisions of others, would have had a substantial effect on the interstate market for wheat.'' [58] In another relevant decision, *Gonzales* v. *Raich,*[59] the Court adopted similar reasoning to uphold the application of the Controlled Substances Act [60] to prohibit the intrastate use of medical marijuana for medicinal purposes. In *Raich,* the Court held that Congress could regulate purely intrastate activity if the failure to do so would ''leave a gaping hole'' in the federal regulatory structure. These cases support the Commission's cross-border authority over swap activities that as a class, or in the aggregate, have a direct and significant connection with activities in, or effect on, U.S. commerce—whether or not an individual swap may satisfy the statutory standard.[61]

(ii) Principles of International Comity

Principles of international comity counsel the government in one country to act reasonably in exercising its jurisdiction with respect to activity that takes place in another country. Statutes should be construed to ''avoid unreasonable interference with the sovereign authority of other nations.'' [62] This rule of construction ''reflects customary principles of international law'' and ''helps the potentially conflicting laws of different nations work together in harmony—a harmony particularly needed in today's highly interdependent commercial world.'' [63]

The Restatement (Third) of Foreign Relations Law of the United States,[64] together with the Restatement (Fourth) of Foreign Relations Law of the United States [65] (collectively, the ''Restatement''), states that a country has jurisdiction to prescribe law with respect to ''conduct outside its territory that has or is intended to have substantial effect within its territory.'' [66] The Restatement also counsels that even where a country has a basis for extraterritorial jurisdiction, it should not prescribe law with respect to a person or activity in another country when the exercise of such jurisdiction is unreasonable.[67]

As a general matter, the Fourth Restatement indicates that the concept of reasonableness as it relates to foreign relations law is ''a principle of statutory interpretation'' that ''operates in conjunction with other principles of statutory interpretation.'' [68] More specifically, the Fourth Restatement characterizes the inquiry into the reasonableness of exercising extraterritorial jurisdiction as an examination into whether ''a genuine connection exists between the state seeking to regulate and the persons, property, or conduct being regulated.'' [69] The Restatement explicitly indicates that the ''genuine connection'' between the state and the person, property, or conduct to be regulated can derive from the effects of the particular conduct or activities in question.[70]

Consistent with the Restatement, the Commission has carefully considered, among other things, the level of the foreign jurisdiction's supervisory interests over the subject activity and the extent to which the activity takes place within the foreign territory. In doing so, the Commission has strived to

[54] The Commission also notes that the Supreme Court has indicated that the FTAIA may be interpreted more broadly when the government is seeking to protect the public from anticompetitive conduct than when a private plaintiff brings suit. *See Hoffman-LaRoche,* 452 U.S. at 170 (''A Government plaintiff, unlike a private plaintiff, must seek to obtain the relief necessary to protect the public from further anticompetitive conduct and to redress anticompetitive harm. And a Government plaintiff has legal authority broad enough to allow it to carry out its mission.'').

[55] The Commission believes this interpretation is supported by Congress's use of the plural term ''activities'' in CEA section 2(i), rather than the singular term ''activity.'' The Commission believes it is reasonable to interpret the use of the plural term ''activities'' in section 2(i) to require not that each particular activity have the requisite connection with U.S. commerce, but rather that such activities in the aggregate, or a class of activity, have the requisite nexus with U.S. commerce. This interpretation is consistent with the overall objectives of Title VII, as described above. Further, the Commission believes that a swap-by-swap approach to jurisdiction would be ''too complex to prove workable.'' *See Hoffman-LaRoche,* 542 U.S. at 168.

[56] *Nat'l Fed'n of Indep. Bus.* v. *Sebelius,* 567 U.S. 519 (2012).

[57] 317 U.S. 111 (1942).

[58] 567 U.S. at 552–53. At issue in *Wickard* was the regulation of a farmer's production and use of wheat even though the wheat was ''not intended in any part for commerce but wholly for consumption on the farm.'' 317 U.S. at 118. The Supreme Court upheld the application of the regulation, stating that although the farmer's ''own contribution to the demand for wheat may be trivial by itself,'' the federal regulation could be applied when his contribution ''taken together with that of many others similarly situated, is far from trivial.'' *Id.* at 128–29. The Court also stated it had ''no doubt that Congress may properly have considered that wheat consumed on the farm where grown, if wholly outside the scheme of regulation, would have a substantial effect in defeating and obstructing its purpose . . ..'' *Id.*

[59] 545 U.S. 1 (2005).

[60] 21 U.S.C. 801 *et seq.*

[61] In *Sebelius,* the Court stated in dicta, ''Where the class of activities is regulated, and that class is within the reach of federal power, the courts have no power to excise, as trivial, individual instances of the class.'' 567 U.S. at 551 (*quoting Perez* v. *United States,* 402 U.S. 146, 154 (1971)). *See also Taylor* v. *U.S.*136 S. Ct. 2074, 2079 (2016) (''[A]ctivities . . . that ''substantially affect'' commerce . . . may be regulated so long as they substantially affect interstate commerce in the aggregate, even if their individual impact on interstate commerce is minimal.'')

[62] *Hoffman-LaRoche,* 542 U.S. at 164.

[63] *Id.* at 165.

[64] Restatement (Third) section 402 cmt. d (1987).

[65] Julian Ku, American Law Institute Approves First Portions of Restatement on Foreign Relations Law (Fourth), OpinioJuris.com, May 22, 2017, *http://opiniojuris.org/2017/05/22/american-law-institute-approves-first-portions-of-restatement-on-foreign-relations-law-fourth/;* Jennifer Morinigo, U.S. Foreign Relations Law, Jurisdiction Approved, ALI Adviser, May 22, 2017, *http://www.thealiadviser.org/us-foreign-relations-law/jurisdiction-approved/;* Restatement (Fourth) of Foreign Relations Law Intro. (Westlaw 2018) (explaining that ''this is only a partial revision'' of the Third Restatement).

[66] Restatement (Fourth) section 409 (Westlaw 2018).

[67] Restatement (Fourth) section 405 cmt. a (Westlaw 2018); *see id.* at section 407 Reporters' Note 3 (''Reasonableness, in the sense of showing a genuine connection, is an important touchstone for determining whether an exercise of jurisdiction is permissible under international law.'').

[68] *Id.* at section 405 cmt. a.

[69] *Id.* at section 407 cmt. a; *see id.* at section 407 Reporters' Note 3.

[70] *Id.* at section 407.

minimize conflicts with the laws of other jurisdictions while seeking, pursuant to section 2(i), to apply the swaps requirements of Title VII to activities outside the United States that have a direct and significant connection with activities in, or effect on, U.S. commerce.

The Commission believes the Final Rule appropriately accounts for these competing interests, ensuring that the Commission can discharge its responsibilities to protect the U.S. markets, market participants, and financial system, consistent with international comity, as set forth in the Restatement. Of particular relevance is the Commission's approach to substituted compliance in the Final Rule, which mitigates burdens associated with potentially conflicting foreign laws and regulations in light of the supervisory interests of foreign regulators in entities domiciled and operating in their own jurisdictions.

E. Final Rule

The Final Rule identifies which cross-border swaps or swap positions a person will need to consider when determining whether it needs to register with the Commission as an SD or MSP, as well as related classifications of swap market participants and swaps (*e.g.,* U.S. person, foreign branch, swap conducted through a foreign branch).[71] Further, the Commission is adopting several tailored exceptions from, and a substituted compliance process for, certain regulations applicable to registered SDs and MSPs. The Final Rule also creates a framework for comparability determinations for such regulations that emphasizes a holistic, outcomes-based approach that is grounded in principles of international comity. Finally, the Final Rule requires SDs and MSPs to create a record of their compliance with the Final Rule and to retain such records in accordance with § 23.203.[72] The Final Rule supersedes the Commission's policy views as set forth in the Guidance with respect to its interpretation and application of section 2(i) of the CEA and the swap provisions addressed in the Final Rule.[73]

Some commenters provided their views on the Proposed Rule generally. AFR and IATP both argued that, in sum, the Proposed Rule would fatally weaken the implementation of Title VII of the Dodd-Frank Act and its application to CFTC-regulated derivatives markets, and urged the Commission to step back from the course outlined in the Proposed Rule and restore elements of the Guidance and the 2016 Proposal that, they maintained, offered better oversight of derivatives markets. The Commission has considered these comments but believes that the Final Rule generally reflects the approach outlined by the Commission in the Guidance, and has determined that it takes account of conflicts with the laws of other jurisdictions when applying the swaps requirements of Title VII to activities outside the United States that have a direct and significant connection with activities in, or effect on, U.S. commerce, permitting the Commission to discharge its responsibilities to protect the U.S. markets, market participants, and financial system, consistent with international comity.

More specifically, the Final Rule takes into account the Commission's experience implementing the Dodd-Frank Act reforms, including its experience with the Guidance and the Cross-Border Margin Rule, comments submitted in connection with the ANE Request for Comment and the Proposed Rule, as well as discussions that the Commission and its staff have had with market participants,[74] other domestic[75] and foreign regulators, and other interested parties. It is essential that a cross-border framework recognize the global nature of the swap market and the supervisory interests of foreign regulators with respect to entities and transactions covered by the Commission's swap regime. In determining the extent to which the Dodd-Frank Act swap provisions addressed by the Final Rule apply to activities outside the United States, the Commission has strived to protect U.S. interests as contemplated by Congress in Title VII, and minimize conflicts with the laws of other jurisdictions. The Commission has carefully considered, among other things, the level of a home jurisdiction's supervisory interests over the subject activity and the extent to which the activity takes place within the home country's territory.[76] At the same time, the Commission has also considered the potential for cross-border activities to have a significant connection with activities in, or effect on, commerce of the United States, as well as the global, highly integrated nature of today's swap markets.

To fulfill the purposes of the Dodd-Frank Act swap reforms, the Commission's supervisory oversight cannot be confined to activities strictly within the territory of the United States. Rather, the Commission will exercise its supervisory authority outside the United States in order to reduce risk to the resiliency and integrity of the U.S. financial system.[77] The Commission will also strive to show deference to non-U.S. regulation when such regulation achieves comparable outcomes to mitigate unnecessary conflict with effective non-U.S. regulatory frameworks and limits fragmentation of the global marketplace.

The Commission has also sought to target those classes of entities whose activities—due to the nature of their relationship with a U.S. person or U.S. commerce—most clearly present the risks addressed by the Dodd-Frank Act provisions, and related regulations covered by the Final Rule. The Final Rule is designed to limit opportunities for regulatory arbitrage by applying the registration thresholds in a consistent manner to differing organizational structures that serve similar economic functions or have similar economic effects. At the same time, the Commission is mindful of the effect of its choices on market efficiency and competition, as well as the importance of international comity when exercising the Commission's authority. The Commission believes that the Final Rule reflects a measured approach that advances the goals underlying SD and MSP regulation, consistent with the Commission's statutory authority, while mitigating market distortions and inefficiencies, and avoiding fragmentation.

II. Key Definitions

The Commission is adopting definitions for certain terms for the purpose of applying the Dodd-Frank Act swap provisions addressed by the Final Rule to cross-border transactions. Certain of these definitions are relevant

[71] There were no MSPs registered with the Commission as of the date of the Final Rule.

[72] *See* Final § 23.23(h)(1).

[73] *See infra* section V for a discussion of certain swap provisions not addressed in the Final Rule.

[74] Summaries of such discussions with market participants are included in the relevant public comment file, available on the Commission's website at *https://comments.cftc.gov/PublicComments/CommentList.aspx?id=3067.*

[75] The Commission has consulted with the Securities and Exchange Commission (''SEC'') and prudential regulators regarding the Final Rule, as required by section 712(a)(1) of the Dodd-Frank Act for the purposes of assuring regulatory consistency and comparability, to the extent possible. Dodd-Frank Act, section 712(a)(1); 15 U.S.C. 8302(a)(1). SEC staff was consulted to increase understanding of each other's regulatory approaches and to harmonize the cross-border approaches of the two agencies to the extent possible, consistent with their respective statutory mandates. As noted in the Entities Rule, the CFTC and SEC intended to address the cross-border application of Title VII in separate releases. *See* Entities Rule, 77 FR at 30628 n.407.

[76] The terms ''home jurisdiction'' or ''home country'' are used interchangeably in this release and refer to the jurisdiction in which the person or entity is established, including the European Union.

[77] *See supra* section I.D.

in assessing whether a person's activities have the requisite ''direct and significant'' connection with activities in, or effect on, U.S. commerce within the meaning of CEA section 2(i). Specifically, the definitions are relevant in determining whether certain swaps or swap positions need to be counted toward a person's SD or MSP threshold and in addressing the cross-border application of certain Dodd-Frank Act requirements (as discussed below in sections III through VII).

A. Reliance on Representations—Generally

The Commission acknowledges that the information necessary for a swap counterparty to accurately assess whether its counterparty or a specific swap meets one or more of the definitions discussed below may be unavailable, or available only through overly burdensome due diligence. For this reason, the Commission believes that a market participant should generally be permitted to reasonably rely on written counterparty representations in each of these respects.[78] Therefore, the Commission proposed that a person may rely on a written representation from its counterparty that the counterparty does or does not satisfy the criteria for one or more of the definitions below, unless such person knows or has reason to know that the representation is not accurate.[79] AFEX/GPS supported the proposed written representation language and noted that it would facilitate compliance with the rules.

The Commission is adopting the ''reliance on representations'' language as proposed.[80] For the purposes of this rule, a person would have reason to know the representation is not accurate if a reasonable person should know, under all of the facts of which the person is aware, that it is not accurate. This language is consistent with: (1) The reliance standard articulated in the Commission's external business conduct rules; [81] (2) the Commission's approach in the Cross-Border Margin Rule; [82] and (3) the reliance standard articulated in the ''U.S. person'' and ''transaction conducted through a foreign branch'' definitions adopted by the SEC in its rule addressing the regulation of cross-border securities-based swap activities (''SEC Cross-Border Rule'').[83] A number of commenters also specifically addressed reliance on representations obtained under the Cross-Border Margin Rule or the Guidance for the ''U.S. person'' and ''Guarantee'' definitions. These comments are addressed below in sections II.B.5 and II.C.

B. U.S. Person, Non-U.S. Person, and United States

1. Generally

(i) Proposed Rule

As discussed in more detail below, the Commission proposed defining ''U.S. person'' consistent with the definition of ''U.S. person'' in the SEC Cross-Border Rule.[84] The proposed definition of ''U.S. person'' was also consistent with the Commission's statutory mandate under the CEA, and in this regard was largely consistent with the definition of ''U.S. person'' in the Cross-Border Margin Rule.[85] Specifically, the Commission proposed to define ''U.S. person'' as:

(1) A natural person resident in the United States;

(2) A partnership, corporation, trust, investment vehicle, or other legal person organized, incorporated, or established under the laws of the United States or having its principal place of business in the United States;

(3) An account (whether discretionary or non-discretionary) of a U.S. person; or

(4) An estate of a decedent who was a resident of the United States at the time of death.[86]

As noted in the Cross-Border Margin Rule,[87] and consistent with the SEC [88] definition of ''U.S. person,'' proposed § 23.23(a)(22)(ii) provided that the principal place of business means the location from which the officers, partners, or managers of the legal person primarily direct, control, and coordinate the activities of the legal person. Consistent with the SEC, the Commission noted that the principal place of business for a collective investment vehicle (''CIV'') would be in the United States if the senior personnel responsible for the implementation of the CIV's investment strategy are located in the United States, depending on the facts and circumstances that are relevant to determining the center of direction, control, and coordination of the CIV.[89]

Additionally, in consideration of the discretionary and appropriate exercise of international comity-based doctrines, proposed § 23.23(a)(22)(iii) stated that the term ''U.S. person'' would not include certain international financial institutions.[90] Specifically, consistent with the SEC's definition,[91] the term U.S. person would not include the International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the United Nations, and their agencies and pension plans, and any other similar international organizations, their agencies, and pension plans.

Further, to provide certainty to market participants, proposed § 23.23(a)(22)(iv) permitted reliance, until December 31, 2025, on any U.S. person-related representations that were obtained to comply with the Cross-Border Margin Rule.[92]

(ii) Summary of Comments

In general, AIMA, AFEX/GPS, Barnard, Chatham, CS, IIB/SIFMA, JFMC/IBAJ, JBA, JSCC, and State Street supported the proposed ''U.S. person'' definition, while IATP generally opposed the proposed definition. Additional comments and suggestions are discussed below.

AIMA, Barnard,[93] Chatham, CS, IIB/SIFMA, JFMC/IBAJ, JSCC, and State Street generally supported the Commission's view that aligning with the SEC's definition of ''U.S. person'' provided consistency to market participants, noting that the harmonized definition would: (1) Provide a consistent approach from operational and compliance perspectives; (2) help avoid undue regulatory complexity for purposes of firms' swaps and security-based swaps businesses; and/or (3) simplify market practice and reduce complexity. AFEX/GPS, Chatham, CS, JFMC/IBAJ, JSCC, and State Street generally stated that the simpler and

[78] Proposed Rule, 85 FR at 958–59; Cross-Border Margin Rule, 81 FR at 34827; Guidance, 78 FR at 45315.

[79] Proposed § 23.23(a); Proposed Rule, 85 FR at 958–59, 1002.

[80] Final § 23.23(a).

[81] *See* 17 CFR 23.402(d).

[82] *See* Cross-Border Margin Rule, 81 FR at 34827.

[83] *See* 17 CFR 240.3a71–3(a)(3)(ii) & (4)(iv); Application of ''Security-Based Swap Dealer'' and ''Major Security-Based Swap Participant'' Definitions to Cross-Border Security-Based Swap Activities; Republication, 79 FR 47278, 47313 (Aug. 12, 2014).

[84] Proposed § 23.23(a)(22); Proposed Rule, 85 FR at 959–63, 1003. *See* 17 CFR 240.3a71–3(a)(4); SEC Cross-Border Rule, 79 FR at 47303–13.

[85] *See* 17 CFR 23.160(a)(10); Cross-Border Margin Rule, 81 FR at 34821–24.

[86] Proposed § 23.23(a)(22)(i); Proposed Rule, 85 FR at 959–63, 1003.

[87] Cross-Border Margin Rule, 81 FR at 34823.

[88] 17 CFR 240.3a71–3(a)(4)(ii).

[89] Proposed § 23.23(a)(22)(ii); Proposed Rule, 85 FR at 960, 1003.

[90] Proposed § 23.23(a)(22)(iii); Proposed Rule, 85 FR at 961–62, 1003.

[91] 17 CFR 240.3a71–3(a)(4)(iii).

[92] Proposed § 23.23(a)(22)(iv); Proposed Rule, 85 FR at 962, 1003.

[93] However, as noted below, Barnard expressed concern regarding other proposed definitions and treatments.

streamlined prongs in the proposed ''U.S. person'' definition allowed for more straightforward application of the definition as compared to the Guidance. Chatham also noted that the proposed definition of ''U.S. person'' establishes a significant nexus to the United States.

FIA recommended that the Commission explicitly state that the scope of the proposed definition of a ''U.S. person'' would not extend to provisions of the CEA governing futures commission merchants (''FCMs'') with respect to both: (1) Exchange-traded futures, whether executed on a designated contract market or a foreign board of trade; and (2) cleared swaps.

IATP suggested restoring the ''U.S. person'' definition from the Guidance and 2016 Proposal. IATP argued that the SEC definition applies to the relatively small universe of security-based swaps, and therefore, the Commission should adopt the ''U.S. person'' and other definitions from the 2016 Proposal for the much larger universe of physical and financial commodity swaps the Commission is authorized to regulate. IATP also asserted that adopting the SEC definition for harmonization purposes was not necessary because SDs and MSPs should have the personnel and information technology resources to comply effectively with reporting and recordkeeping of swaps and security-based swaps. Further, any reduced efficiency would be compensated for by having the ''U.S. person'' definition apply not only to enumerated entities but to a non-exhaustive listing that anticipates the creation of new legal entities engaged in swaps activities.

(iii) Final Rule

As discussed in more detail below, the Commission is adopting the ''U.S. person'' definition as proposed, with certain clarifications.[94] In response to IATP, the Commission continues to be of the view that harmonization of the ''U.S. person'' definition with the SEC is the appropriate approach given that it is straightforward to apply compared to the Guidance definition, and will capture substantially the same types of entities as the ''U.S. person'' definition in the Cross-Border Margin Rule.[95] In addition, harmonizing with the definition in the SEC Cross-Border Rule is not only consistent with section 2(i) of the CEA,[96] but is also expected to reduce undue compliance costs for market participants. Therefore, as noted by several commenters, the definition will reduce complexity for entities that are participants in the swaps and security-based swaps markets and may register both as SDs with the Commission and as security-based swap dealers with the SEC. The Commission is also of the view that the ''U.S. person'' definition in the Cross-Border Margin Rule largely encompasses the same universe of persons as the definition used in the SEC Cross-Border Rule and the Final Rule.[97]

In response to FIA, pursuant to § 23.23(a), ''U.S. person'' only has the meaning in the definition for the purposes of § 23.23. However, to be clear that the definition of ''U.S. person'' is only applicable for purposes of the Final Rule, the rule now includes the word ''solely'' and reads ''*Solely* for purposes of this section . . . .''

Generally, the Commission believes that the definition offers a clear, objective basis for determining which individuals or entities should be identified as U.S. persons for purposes of the swap requirements addressed by the Final Rule. Specifically, the various prongs, as discussed in more detail below, are intended to identify persons whose activities have a significant nexus to the United States by virtue of their organization or domicile in the United States.[98]

Additionally, the Commission is adopting as proposed the definitions for ''non-U.S. person,'' ''United States,'' and ''U.S.'' The term ''non-U.S. person'' means any person that is not a U.S. person.[99] Further, the Final Rule defines ''United States'' and ''U.S.'' as the United States of America, its territories and possessions, any State of the United States, and the District of Columbia.[100] The Commission did not receive any comments regarding these definitions.

2. Prongs

As the Commission noted in the Proposed Rule, paragraph (i) of the ''U.S. person'' definition identifies certain persons as a ''U.S. person'' by virtue of their domicile or organization within the United States.[101] The Commission has traditionally looked to where legal entities are organized or incorporated (or in the case of natural persons, where they reside) to determine whether they are U.S. persons.[102] In the Commission's view, these persons—by virtue of their decision to organize or locate in the United States and because they are likely to have significant financial and legal relationships in the United States—are appropriately included within the definition of ''U.S. person.'' [103]

(i) § 23.23(a)(23)(i)(A) and (B)

Paragraphs (i)(A) and (B) of the ''U.S. person'' definition generally incorporate a ''territorial'' concept of a U.S. person.[104] That is, these are natural persons and legal entities that are physically located or incorporated within U.S. territory, and thus are subject to the Commission's jurisdiction. Further, the Commission generally considers swap activities where such persons are counterparties, as a class and in the aggregate, as satisfying the ''direct and significant'' test under CEA section 2(i). Consistent with the ''U.S. person'' definition in the Cross-Border Margin Rule[105] and the SEC Cross-Border Rule,[106] the definition encompasses both foreign and domestic branches of an entity. As discussed below, a branch does not have a legal identity apart from its principal entity.[107]

[94] Final § 23.23(a)(23). Note that due to renumbering, the paragraph references for the definitions in § 23.23(a) of the Final Rule vary from the paragraph references in the Proposed Rule.

[95] *See* Proposed Rule, 85 FR at 959.

[96] Harmonizing the Commission's definition of ''U.S. person'' with the definition in the SEC Cross-Border Rule also is consistent with the dictate in section 712(a)(7) of the Dodd-Frank Act that the CFTC and SEC ''treat functionally or economically similar'' SDs, MSPs, security-based swap dealers, and major security-based swap participants ''in a similar manner.'' Dodd-Frank Act, section 712(a)(7)(A); 15 U.S.C. 8307(a)(7)(A). *See* Proposed Rule, 85 FR at 959.

[97] *See* Cross-Border Margin Rule, 81 FR at 34824. The Final Rule defines ''U.S. person'' in a manner that is substantially similar to the definition used by the SEC in the context of cross-border regulation of security-based swaps. Proposed Rule, 85 FR at 959.

[98] Proposed Rule, 85 FR at 959.

[99] Final § 23.23(a)(10).

[100] Final § 23.23(a)(20).

[101] Proposed Rule, 85 FR at 959.

[102] Cross-Border Margin Rule, 81 FR at 34823; Proposed Rule, 85 FR at 959. *See also* 17 CFR 4.7(a)(1)(iv) (defining ''Non-United States person'' for purposes of part 4 of the Commission regulations relating to commodity pool operators (''CPOs'')).

[103] Proposed Rule, 85 FR at 959.

[104] *Id.*

[105] *See* 17 CFR 23.160(a)(10)(iii) (U.S. person includes a corporation, partnership, limited liability company, business or other trust, association, joint-stock company, fund or any form of entity similar to any of the foregoing (other than an entity described in paragraph (a)(10)(iv) or (v) of this section) (a legal entity), in each case that is organized or incorporated under the laws of the United States or that has its principal place of business in the United States, *including any branch of such legal entity*) (emphasis added).

[106] *See* SEC Cross-Border Rule, 79 FR at 47308 (''[T]he final definition determines a legal person's status at the entity level and thus applies to the entire legal person, including any foreign operations that are part of the U.S. legal person. Consistent with this approach, a foreign branch, agency, or office of a U.S. person is treated as part of a U.S. person, as it lacks the legal independence to be considered a non-U.S. person for purposes of Title VII even if its head office is physically located within the United States.'').

[107] *See* Proposed Rule, 85 FR at 959.

The first prong of the proposed definition stated that a natural person resident in the United States would be considered a U.S. person. No comments were received regarding the first prong of the ''U.S. person'' definition and the Commission is adopting it as proposed.[108]

The second prong of the proposed definition stated that a partnership, corporation, trust, investment vehicle, or other legal person organized, incorporated, or established under the laws of the United States or having its principal place of business in the United States would be considered a U.S. person. In the Proposed Rule, the Commission stated that the second prong of the definition would subsume the pension fund and trust prongs of the ''U.S. person'' definition in the Cross-Border Margin Rule.[109] No comments were received regarding this aspect of the Proposed Rule and the Commission is adopting it as proposed.[110]

Specifically, the Commission is of the view that, as adopted, § 23.23(a)(23)(i)(B) includes in the definition of the term ''U.S. person'' pension plans for the employees, officers, or principals of a legal entity described in § 23.23(a)(23)(i)(B), which is a separate prong in the Cross-Border Margin Rule.[111] Although the SEC Cross-Border Rule directly addresses pension funds only in the context of international financial institutions, discussed below, the Commission believes it is important to clarify that pension funds in other contexts could meet the requirements of § 23.23(a)(23)(i)(B).[112]

Additionally, § 23.23(a)(23)(i)(B) subsumes the trust prong of the ''U.S. person'' definition in the Cross-Border Margin Rule.[113] With respect to trusts addressed in § 23.23(a)(23)(i)(B), the Commission expects that its approach is consistent with the manner in which trusts are treated for other purposes under the law. The Commission has considered that each trust is governed by the laws of a particular jurisdiction, which may depend on steps taken when the trust was created or other circumstances surrounding the trust. The Commission believes that if a trust is governed by U.S. law (*i.e.,* the law of a state or other jurisdiction in the United States), then it is generally reasonable to treat the trust as a U.S. person for purposes of the Final Rule. Another relevant element in this regard is whether a court within the United States is able to exercise primary supervision over the administration of the trust. The Commission expects that this aspect of the definition generally aligns the treatment of the trust for purposes of the Final Rule with how the trust is treated for other legal purposes. For example, the Commission expects that if a person could bring suit against the trustee for breach of fiduciary duty in a U.S. court (and, as noted above, the trust is governed by U.S. law), then treating the trust as a U.S. person is generally consistent with its treatment for other purposes.[114]

(ii) § 23.23(a)(23)(i)(D)

Under the fourth prong of the proposed definition, an estate of a decedent who was a resident of the United States at the time of death would be included in the definition of ''U.S. person.'' No comments were received regarding this aspect of the Proposed Rule and the Commission is adopting it as proposed.[115] With respect to § 23.23(a)(23)(i)(D), the Commission believes that the swaps of a decedent's estate should generally be treated the same as the swaps entered into by the decedent during their life.[116] If the decedent was a party to any swaps at the time of death, then those swaps should generally continue to be treated in the same way after the decedent's death, at which time the swaps would most likely pass to the decedent's estate. Also, the Commission expects that this prong will be predictable and straightforward to apply for natural persons planning for how their swaps will be treated after death, for executors and administrators of estates, and for the swap counterparties to natural persons and estates.

(iii) § 23.23(a)(23)(i)(C)

The third prong of the definition, the ''account'' prong, was proposed to ensure that persons described in prongs (A), (B), and (D) of the definition would be treated as U.S. persons even if they use discretionary or non-discretionary accounts to enter into swaps, irrespective of whether the person at which the account is held or maintained is a U.S. person.[117] Consistent with the Cross-Border Margin Rule, the Commission stated that this prong would apply for individual or joint accounts.[118] IIB/SIFMA recommended that, consistent with the SEC, the Commission clarify that under the ''account'' prong of the definition, an account's U.S. person status should depend on whether any U.S.-person owner of the account actually incurs obligations under the swap in question.

The Commission is adopting this aspect of the U.S. person definition as proposed, with a clarification.[119] In response to the IIB/SIFMA comment, the Commission is clarifying that an account's U.S. person status depends on whether any U.S. person owner of the account actually incurs obligations under the swap in question. Consistent with the SEC Cross-Border Rule, where an account is owned by both U.S. persons and non-U.S. persons, the U.S.-person status of the account, as a general matter, turns on whether any U.S.-person owner of the account incurs obligations under the swap.[120] Neither the status of the fiduciary or other person managing the account, nor the discretionary or non-discretionary nature of the account, nor the status of the person at which the account is held or maintained, are relevant in determining the account's U.S.-person status.

(iv) Exclusion of Unlimited U.S. Responsibility Prong

Unlike the Cross-Border Margin Rule, the proposed definition of ''U.S. person'' did not include certain legal entities that are owned by one or more U.S. person(s) and for which such person(s) bear unlimited responsibility for the obligations and liabilities of the legal entity (''unlimited U.S. responsibility'' prong).[121] The Commission invited comment on whether it should include an unlimited U.S. responsibility prong in the definition of ''U.S. person,'' and if not, whether it should revise its interpretation of ''guarantee'' in a manner consistent with the SEC such that persons that would have been considered U.S. persons pursuant to an unlimited U.S. responsibility prong would instead be considered entities with guarantees from a U.S. person.[122]

Chatham and IIB/SIFMA agreed that the Commission should not include an unlimited U.S. responsibility prong in the ''U.S. Person'' definition, noting that

[108] Final § 23.23(a)(23)(i)(A).

[109] Proposed Rule, 85 FR at 959–60. *See* 17 CFR 23.160(a)(10)(iv) and (v).

[110] Final § 23.23(a)(23)(i)(B).

[111] *See* 17 CFR 23.160(a)(10)(iv).

[112] Proposed Rule, 85 FR at 959.

[113] *See* 17 CFR 23.160(a)(10)(v).

[114] Proposed Rule, 85 FR at 959–60.

[115] Final § 23.23(a)(23)(i)(D).

[116] Proposed Rule, 85 FR at 960.

[117] *Id.*

[118] *Id. See* 17 CFR 23.160(a)(10)(vii).

[119] Final § 23.23(a)(23)(i)(C).

[120] *See* SEC Cross-Border Rule, 79 FR at 47312.

[121] Proposed Rule, 85 FR at 961. *See* 17 CFR 23.160(a)(10)(vi); Cross-Border Margin Rule, 81 FR at 34823–34824. *See also* Guidance, 78 FR at 45312–13 (discussing the unlimited U.S. responsibility prong for purposes of the Guidance).

[122] Proposed Rule, 85 FR at 969.

the persons that would be captured under the prong are corporate structures that are not commonly in use in the marketplace (*e.g.,* unlimited liability corporations, general partnerships, and sole proprietorships). IIB/SIFMA added that to the extent a firm uses this structure, the Commission can sufficiently address the resulting risks to the United States by treating the firm as having a guarantee from a U.S. person, as the SEC does.

The Commission is adopting as proposed a definition of ''U.S. person'' that does not include an unlimited U.S. responsibility prong. Although this corporate structure may exist in some limited form, the Commission does not believe that justifies the cost of classification as a ''U.S. person.'' This prong was designed to capture persons that could give rise to risk to the U.S. financial system in the same manner as with non-U.S. persons whose swap transactions are subject to explicit financial support arrangements from U.S. persons.[123] Rather than including this prong in its ''U.S. person'' definition, the SEC took the view that when a non-U.S. person's counterparty has recourse to a U.S. person for the performance of the non-U.S. person's obligations under a security-based swap by virtue of the U.S. person's unlimited responsibility for the non-U.S. person, the non-U.S. person would be required to include the security-based swap in its security-based swap dealer (if it is a dealing security-based swap) and major security-based swap participant threshold calculations as a guarantee.[124] Therefore, as discussed below with respect to the definition of ''guarantee,'' the Commission is clarifying that legal entities that are owned by one or more U.S. person(s) and for which such person(s) bear unlimited responsibility for the obligations and liabilities will be considered as having a guarantee from a U.S. person, similar to the approach in the SEC Cross-Border Rule. The CFTC's anti-evasion rules address concerns that persons may structure transactions to avoid classification as a U.S. person.[125]

The treatment of the unlimited U.S. liability prong in the Final Rule does not affect an entity's obligations with respect to the Cross-Border Margin Rule. To the extent that entities are considered U.S. persons for purposes of the Cross-Border Margin Rule as a result of the unlimited U.S. liability prong, the Commission believes that the different purpose of the registration-related rules justifies this potentially different treatment.[126]

(v) Exclusion of Collective Investment Vehicle Prong

Consistent with the definition of ''U.S. person'' in the Cross-Border Margin Rule and the SEC Cross-Border Rule, the proposed definition did not include a commodity pool, pooled account, investment fund, or other CIV that is majority-owned by one or more U.S. persons.[127] This prong was included in the Guidance definition. The Commission invited comment on whether it is appropriate that commodity pools, pooled accounts, investment funds, or other CIVs that are majority-owned by U.S. persons would not be included in the proposed definition of ''U.S. person.''[128]

AIMA, Chatham, IIB/SIFMA, JFMC/IBAJ,[129] JBA, and State Street supported not including this prong in the ''U.S. person'' definition. They generally noted that there are practical difficulties in tracking the beneficial ownership in CIVs, and therefore, including a CIV prong would increase the complexity of the ''U.S. person'' definition. AIMA stated that this could necessitate conservative assumptions being made to avoid the risk of breaching regulatory requirements that depend on the status of investors in the vehicle. JBA noted that non-U.S. persons may choose not to enter into transactions with CIVs in which U.S. persons are involved to avoid the practical burdens of identifying and tracking the beneficial ownership of funds in real-time and the excessive cost arising from the registration threshold calculations. JFMC/IBAJ elaborated that ownership composition can change throughout the life of the vehicle due to redemptions and additional investments.

AIMA, Chatham, and State Street also noted that there are limited benefits to including a requirement to ''look-through'' non-U.S. CIVs to identify and track U.S. beneficial owners of such vehicles. AIMA stated that it is reasonable to assume that the potential investment losses to which U.S. investors in CIVs are exposed are limited to their initial capital investment. Chatham stated that the composition of a CIV's beneficial owners is not likely to have a significant bearing on the degree of risk that the CIV's swap activity poses to the U.S. financial system, noting that CIVs organized or having a principal place of business in the U.S. would be under the Commission's authority, and majority-owned CIVs may be subject to margin requirements in foreign jurisdictions.

AIMA added that the definition of ''U.S. person'' in the Guidance is problematic for certain funds managed by investment managers because they are subject to European rules on clearing, margining, and risk mitigation.

After consideration of the comments, and consistent with the definition of ''U.S. person'' in the Cross-Border Margin Rule and the SEC Cross-Border Rule, the Commission is adopting as proposed a ''U.S. person'' definition that does not include a commodity pool, pooled account, investment fund, or other CIV that is majority-owned by one or more U.S. persons.[130] Similar to the SEC, the Commission is of the view that including majority-owned CIVs within the definition of ''U.S. person'' for the purposes of the Final Rule would likely cause more CIVs to incur additional programmatic costs associated with the relevant Title VII requirements and ongoing assessments, while not significantly increasing programmatic benefits given that the composition of a CIV's beneficial owners is not likely to have significant bearing on the degree of risk that the CIV's swap activity poses to the U.S. financial system.[131] Although many of these CIVs have U.S. participants that could be adversely affected in the event of a counterparty default, systemic risk concerns are mitigated to the extent these CIVs are subject to margin requirements in foreign jurisdictions. In addition, the exposure of participants to losses in CIVs is typically limited to their investment amount, and it is unlikely that a participant in a CIV would make counterparties whole in the event of a default.[132] Further, the Commission continues to believe that identifying and tracking a CIV's beneficial ownership may pose a significant challenge, particularly in certain circumstances such as fund-of-funds or master-feeder structures.[133] Therefore, although the U.S. participants in such CIVs may be adversely affected in the event of a counterparty default, the Commission has determined that the majority-

[123] *Id.* at 960–961.

[124] SEC Cross-Border Rule, 79 FR at 47308 n.255, 47316–47317.

[125] *See* 17 CFR 1.6.

[126] Proposed Rule, 85 FR at 961.

[127] *Id. See* Cross-Border Margin Rule, 81 FR at 34824; SEC Cross-Border Rule, 79 FR at 47311, 47337.

[128] Proposed Rule, 85 FR at 969.

[129] JFMC/IBAJ also requested that conforming amendments be made to the ''U.S. person'' definition under the Cross-Border Margin Rule. However, this comment is outside of the scope of the Final Rule.

[130] *See* Cross-Border Margin Rule, 81 FR at 34824; SEC Cross-Border Rule, 79 FR at 47311, 47337.

[131] Proposed Rule, 85 FR at 961. *See* SEC Cross-Border Rule, 79 FR at 47337.

[132] Proposed Rule, 85 FR at 961; SEC Cross-Border Rule, 79 FR at 47311.

[133] *See* Cross-Border Margin Rule, 81 FR at 34824.

ownership test should not be included in the definition of ''U.S. person.''

A CIV fitting within the majority U.S. ownership prong may also be a U.S. person within the scope of § 23.23(a)(23)(i)(B) of the Final Rule (entities organized or having a principal place of business in the United States). As the Commission clarified in the Cross-Border Margin Rule, whether a pool, fund, or other CIV is publicly offered only to non-U.S. persons and not offered to U.S. persons is not relevant in determining whether it falls within the scope of the ''U.S. person'' definition.[134]

(vi) Exclusion of Catch-All Prong

Unlike the non-exhaustive ''U.S. person'' definition provided in the Guidance,[135] the Commission proposed that the definition of ''U.S. person'' be limited to persons enumerated in the rule, consistent with the Cross-Border Margin Rule and the SEC Cross-Border Rule.[136] The Commission invited comment on whether the ''U.S. person'' definition should include a catch-all provision.[137]

AFEX/GPS, Chatham, IIB/SIFMA, and JBA supported elimination of the ''include, but not limited to'' language from the Guidance. AFEX/GPS stated that this approach should help facilitate compliance with Commission rules. Chatham stated that the catch-all prong works against the core purposes of the cross-border rules, to enhance regulatory cooperation and transparency. IIB/SIFMA stated that market participants have lacked any practical way to delineate the scope of that catch-all phrase, leading to legal uncertainty. JBA stated that the provision is difficult to interpret and leads to uncertainty, and potentially reduced transactions by market participants, leading to increased bifurcation in the market.

The Commission is adopting this aspect of the ''U.S. person'' definition as proposed.[138] Unlike the non-exhaustive ''U.S. person'' definition provided in the Guidance, the definition of ''U.S. person'' is limited to persons enumerated in the rule, consistent with the Cross-Border Margin Rule and the SEC Cross-Border Rule.[139] The Commission believes that the prongs adopted in the Final Rule capture those persons with sufficient jurisdictional nexus to the U.S. financial system and commerce in the United States that they should be categorized as ''U.S. persons.''[140]

3. Principal Place of Business

The Commission proposed to define ''principal place of business'' as the location from which the officers, partners, or managers of the legal person primarily direct, control, and coordinate the activities of the legal person, consistent with the SEC definition of ''U.S. person.''[141] Additionally, with respect to a CIV, the Proposed Rule stated that this location is the office from which the manager of the CIV primarily directs, controls, and coordinates the investment activities of the CIV, and noted that activities such as formation of the CIV, absent an ongoing role by the person performing those activities in directing, controlling, and coordinating the investment activities of the CIV, generally would not be as indicative of activities, financial and legal relationships, and risks within the United States of the type that Title VII is intended to address as the location of a CIV manager.[142] The Commission invited comment on whether, when determining the principal place of business for a CIV, the Commission should consider including as a factor whether the senior personnel responsible for the formation and promotion of the CIV are located in the United States, similar to the approach in the Cross-Border Margin Rule.[143]

AIMA supported the proposed definition of ''principal place of business'' and stated that there are more relevant indicia of U.S. nexus than the activities of forming and promoting a CIV, such as the location of staff who control the investment activities of the CIV. Similarly, IIB/SIFMA supported adopting the SEC's ''principal place of business'' test for CIVs because it better captures business reality by focusing more on investment strategy rather than the location of promoters who do not have an ongoing responsibility for the vehicle.

The Commission is adopting the ''principal place of business'' aspect of the ''U.S. person'' definition as proposed.[144] As noted in the Cross-Border Margin Rule,[145] and consistent with the SEC definition of ''U.S. person,''[146] § 23.23(a)(23)(ii) provides that the principal place of business means the location from which the officers, partners, or managers of the legal person primarily direct, control, and coordinate the activities of the legal person. With the exception of externally managed entities, as discussed below, the Commission is of the view that for most entities, the location of these officers, partners, or managers generally corresponds to the location of the person's headquarters or main office. However, the Commission believes that a definition that focuses exclusively on whether a legal person is organized, incorporated, or established in the United States could encourage some entities to move their place of incorporation to a non-U.S. jurisdiction to avoid complying with the relevant Dodd-Frank Act requirements, while maintaining their principal place of business—and therefore, risks arising from their swap transactions—in the United States. Moreover, a ''U.S. person'' definition that does not include a ''principal place of business'' element could result in certain entities falling outside the scope of the relevant Dodd-Frank Act-related requirements, even though the nature of their legal and financial relationships in the United States is, as a general matter, indistinguishable from that of entities incorporated, organized, or established in the United States. Therefore, the Commission is of the view that it is appropriate to treat such entities as U.S. persons for purposes of the Final Rule.[147]

However, determining the principal place of business of a CIV, such as an investment fund or commodity pool, may require consideration of additional factors beyond those applicable to operating companies.[148] The Commission interprets that, for an externally managed investment vehicle, this location is the office from which the manager of the vehicle primarily directs, controls, and coordinates the investment activities of the vehicle.[149] This interpretation is consistent with the Supreme Court's decision in *Hertz Corp.* v. *Friend,* which described a corporation's principal place of business, for purposes of diversity jurisdiction, as the ''place where the corporation's high level officers direct, control, and coordinate the

[134] *Id.* at 34824 n.62.

[135] *See* Guidance, 78 FR at 45316.

[136] Proposed Rule, 85 FR at 961. *See* 17 CFR 23.160(a)(10); 17 CFR 240.3a71–3(a)(4); Cross-Border Margin Rule, 81 FR at 34824.

[137] Proposed Rule, 85 FR at 969.

[138] *Id.* at 961.

[139] *See* 17 CFR 23.160(a)(10); 17 CFR 240.3a71–3(a)(4); Cross-Border Margin Rule, 81 FR at 34824; Guidance, 78 FR at 45316 (discussing the inclusion of the prefatory phrase ''include, but not be limited to'' in the interpretation of ''U.S. person'' in the Guidance).

[140] Proposed Rule, 85 FR at 961.

[141] Proposed § 23.23(a)(22)(ii); Proposed Rule, 85 FR at 960, 1003. *See* 17 CFR 240.3a71–3(a)(4)(ii).

[142] Proposed Rule, 85 FR at 960.

[143] *Id.* at 969.

[144] Final § 23.23(a)(23)(ii).

[145] Cross-Border Margin Rule, 81 FR at 34823.

[146] 17 CFR 240.3a71–3(a)(4)(ii).

[147] *See* Proposed Rule, 85 FR at 960; SEC Cross-Border Rule, 79 FR at 47309.

[148] Proposed Rule, 85 FR at 960.

[149] Final § 23.23(a)(23)(ii).

corporation's activities.'' [150] In the case of a CIV, the senior personnel that direct, control, and coordinate a CIV's activities are generally not the named directors or officers of the CIV, but rather persons employed by the CIV's investment advisor or promoter, or in the case of a commodity pool, its CPO. Therefore, consistent with the SEC Cross-Border Rule,[151] when a primary manager is responsible for directing, controlling, and coordinating the overall activity of a CIV, the CIV's principal place of business under the Final Rule is the location from which the manager carries out those responsibilities.

Under the Cross-Border Margin Rule,[152] the Commission generally considers the principal place of business of a CIV to be in the United States if the senior personnel responsible for either: (1) The formation and promotion of the CIV; or (2) the implementation of the CIV's investment strategy are located in the United States, depending on the facts and circumstances that are relevant to determining the center of direction, control, and coordination of the CIV. Although the second prong is consistent with the approach discussed above, the Commission does not believe that activities such as formation of the CIV, absent an ongoing role by the person performing those activities in directing, controlling, and coordinating the investment activities of the CIV, generally will be as indicative of activities, financial and legal relationships, and risks within the United States of the type that Title VII is intended to address as the location of a CIV manager.[153] The Commission may also consider amending the ''U.S. person'' definition in the Cross-Border Margin Rule in the future.

4. Exception for International Financial Institutions

The Commission proposed that, in consideration of the discretionary and appropriate exercise of international comity-based doctrines, the term ''U.S. person'' would not include certain multilateral and other international financial institutions.[154]

IIB/SIFMA supported the proposed exception for certain international financial institutions, noting that the Commission has routinely recognized the special status afforded these institutions under the traditions of the international system by effectively treating them as non-U.S. persons for most purposes, and it is therefore appropriate for the Commission to codify this treatment through this exception. IIB/SIFMA also stated that the catch-all for ''similar international organizations'' appropriately addresses the international comity considerations that underlie this exception.

The Commission is adopting this aspect of the ''U.S. person'' definition as proposed, with a technical modification as discussed below.[155] Consistent with the SEC's definition,[156] the term ''U.S. person'' does not include the International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the United Nations, and their agencies and pension plans, and any other similar international organizations, and their agencies and pension plans. The Commission believes that although such foreign entities are not necessarily immune from U.S. jurisdiction for commercial activities undertaken with U.S. counterparties or in U.S. markets, the sovereign or international status of such international financial institutions that themselves participate in the swap markets in a commercial manner is relevant in determining whether such entities should be treated as U.S. persons, regardless of whether any of the prongs of the definition apply.[157] There is nothing in the text or history of the swap-related provisions of Title VII to suggest that Congress intended to deviate from the traditions of the international system by including such international financial institutions within the definitions of the term ''U.S. person.''

Consistent with the Entities Rule and the Guidance, the Commission interprets the term ''international financial institutions'' to include the ''international financial institutions'' that are defined in 22 U.S.C. 262r(c)(2) and institutions defined as ''multilateral development banks'' in the European Union's regulation on ''OTC derivatives, central counterparties and trade repositories.'' [158] Reference to 22 U.S.C. 262r(c)(2) and the European Union definition is consistent with Commission precedent in the Entities Rule.[159] Both of those definitions identify many of the entities for which discretionary and appropriate exercise of international comity-based doctrines is appropriate with respect to the ''U.S. person'' definition.[160] This prong also includes institutions identified in CFTC Staff Letters 17–34 [161] and 18–13.[162] In CFTC Staff Letter 17–34, Commission staff provided relief from CFTC margin requirements to swaps between SDs and the European Stability Mechanism (''ESM''),[163] and in CFTC Staff Letter

[150] 559 U.S. 77, 80 (2010). *See* Proposed Rule, 85 FR at 960; Cross-Border Margin Rule, 81 FR at 34823.

[151] *See* SEC Cross-Border Rule, 79 FR at 47310–47311.

[152] Cross-Border Margin Rule, 81 FR at 34823.

[153] Proposed Rule, 85 FR at 960.

[154] Proposed § 23.23(a)(22)(iii); Proposed Rule, 85 FR at 961–962, 1003.

[155] Final § 23.23(a)(23)(iii).

[156] *See* 17 CFR 240.3a71–3(a)(4)(iii).

[157] Proposed Rule, 85 FR at 961–962. *See, e.g.,* Entities Rule, 77 FR at 30692–30693 (discussing the application of the ''swap dealer'' and ''major swap participant'' definitions to foreign governments, foreign central banks, and international financial institutions). *See also* Guidance, 78 FR at 45353 n.531.

[158] Regulation (EU) No 648/2012 of the European Parliament and of the Council on OTC Derivative Transactions, Central Counterparties and Trade Repositories, Article 1(5(a)) (July 4, 2012), available at *https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32012R0648.* Article 1(5(a)) references Section 4.2 of Part 1 of Annex VI to Directive 2006/48/EC, available at *https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32006L0048.*

[159] Entities Rule, 77 FR at 30692 n.1180. The Guidance referenced the Entities Rule's interpretation as well. Guidance, 78 FR at 45353 n.531.

[160] The definitions overlap but together include the following: The International Monetary Fund, International Bank for Reconstruction and Development, European Bank for Reconstruction and Development, International Development Association, International Finance Corporation, Multilateral Investment Guarantee Agency, African Development Bank, African Development Fund, Asian Development Bank, Inter-American Development Bank, Bank for Economic Cooperation and Development in the Middle East and North Africa, Inter-American Investment Corporation, Council of Europe Development Bank, Nordic Investment Bank, Caribbean Development Bank, European Investment Bank and European Investment Fund. Note that the International Bank for Reconstruction and Development, the International Development Association, the International Finance Corporation, and the Multilateral Investment Guarantee Agency are parts of the World Bank Group.

[161] *See* CFTC Staff Letter No. 17–34, Commission Regulations 23.150–159, 161: No-Action Position with Respect to Uncleared Swaps with the European Stability Mechanism (Jul, 24, 2017), available at *https://www.cftc.gov/sites/default/files/idc/groups/public/@lrlettergeneral/documents/letter/17-34.pdf. See also* CFTC Staff Letter No. 19–22, Commission Regulations 23.150–159, 23.161: Revised No-Action Position with Respect to Uncleared Swaps with the European Stability Mechanism (Oct. 16, 2019), available at *https://www.cftc.gov/csl/19-22/download.*

[162] *See* CFTC Staff Letter No. 18–13, No-Action Position: Relief for Certain Non-U.S. Persons from Including Swaps with International Financial Institutions in Determining Swap Dealer and Major Swap Participant Status (May 16, 2018), available at *https://www.cftc.gov/sites/default/files/csl/pdfs/18/18-13.pdf.*

[163] *See* CFTC Staff Letter No. 17–34. In addition, in May 2020, the Commission adopted an amendment to § 23.151 to exclude ESM from the definition of ''financial end user,'' which will have the effect of excluding swaps between certain SDs and ESM from the Commission's uncleared swap margin requirements. *See* Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 85 FR 27674 (May 11, 2020).

18–13, Commission staff identified the North American Development Bank (''NADB'') as an additional entity that should be considered an international financial institution for purposes of applying the SD and MSP definitions.[164] Interpreting the definition to include the two entities identified in CFTC Staff Letters 17–34 and 18–13 is consistent with the discretionary and appropriate exercise of international comity because the status of both entities is similar to that of the other international financial institutions identified in the Entities Rule. Consistent with the SEC definition of ''U.S. person,'' the Final Rule lists specific international financial institutions but also provides a catch-all for ''any other similar international organizations, and their agencies and pension plans.'' As a technical edit, the Commission notes that the catch-all for international financial institutions in the Final Rule now includes ''and'' in the clause ''*and* their agencies and pension plans.'' The catch-all provision extends to any of the entities discussed above that are not explicitly listed in the Final Rule.[165]

5. Reliance on Prior Representations

As noted above in section II.A, the Final Rule states that a person may rely on a written representation from its counterparty that the counterparty does or does not satisfy the criteria for one or more of the definitions, unless such person knows or has reason to know that the representation is not accurate.[166]

Further, with respect to the ''U.S. person'' definition, to provide certainty to market participants, the Commission proposed to permit reliance, until December 31, 2025, on any U.S. person-related representations that were obtained to comply with the Cross-Border Margin Rule.[167] The Commission also stated that any person designated as a ''U.S. person'' under the Proposed Rule would also be a ''U.S. person'' under the Guidance, and therefore, market participants would also be able to rely on representations previously obtained under the ''U.S. person'' definition in the Guidance.[168]

IIB/SIFMA and State Street recommended that the reliance on U.S. person representations made with respect to the Cross-Border Margin Rule should be permitted on a permanent basis. State Street asserted that permanent relief raises no new policy considerations, eliminates a ''cliff effect'' in 2025, and eliminates the potential need for market participants to seek Commission extension of the 2025 deadline should circumstances arise where seeking new representations is impractical or unduly burdensome. Additionally, IIB/SIFMA, ISDA, JFMC/IBAJ, and State Street stated that reliance should explicitly be permitted with respect to representations made pursuant to the Guidance. JFMC/IBAJ stated that this would be appropriate given the compliance burdens associated with obtaining representations. State Street noted that the Commission would increase clarity and market efficiency by explicitly providing for Guidance-related representations in final rule text.

In response to these comments, the Commission notes that it proposed temporary reliance on prior representations in the Proposed Rule because it assumed that SDs and MSPs somewhat routinely amend swap trading relationship documentation and thus updated representations based on the proposed U.S. person definition could be obtained in the course of these routine amendments. Permitting temporary reliance to facilitate this method of updating representations is less burdensome and more cost efficient than requiring all affected SDs and MSPs to update representations within a relatively brief compliance period. The Commission has determined that permanent reliance on representations obtained under the Guidance or the Cross-Border Margin Rule would be contrary to good recordkeeping practices, particularly for dormant relationships, which require updated representations within a set time period. Additionally, there are a variety of circumstances that routinely lead SDs and MSPs to amend counterparty trading relationship documentation, such as address changes, payment detail updates, ISDA definition changes, and LIBOR amendments.

To relieve concerns that the December 31, 2025 deadline is burdensome, the Commission is adopting an approximately seven year time limit, until December 31, 2027, for reliance on ''U.S. person'' representations made pursuant to the Cross-Border Margin Rule, instead of the five year limit that was proposed.[169] Thus, for those counterparties for whom a person has already obtained U.S. person-related representations under the Cross-Border Margin Rule, U.S. person-related representations under the Final Rule will only be required from those counterparties with whom swaps are entered after December 31, 2027. Nevertheless, best practice is to obtain updated representations as soon as practicable.

In addition, the Commission has adjusted the rule text of § 23.23(a)(23)(iv) to clarify that reliance is only permitted for representations obtained prior to the effective date of the Final Rule.[170] Persons should not be permitted to rely on representations obtained pursuant to the Cross-Border Margin Rule after the effective date of the Final Rule when such persons could have also obtained representations pursuant to the Final Rule contemporaneously therewith.

The Commission reiterates that it believes that any person designated as a ''U.S. person'' under the Final Rule is also a ''U.S. person'' under the Guidance definition, as the Final Rule's definition is narrower in scope. Therefore, the Commission is of the view that market participants may also rely on representations previously obtained using the ''U.S. person'' definition in the Guidance.[171] A representation obtained under the Guidance should not be relied on permanently, and new representations should be obtained as soon as practicable, but in the Commission's view it would not be appropriate to rely on representations under the Guidance after the December 31, 2027 deadline for similar representations made under the Cross-Border Margin Rule. Thus, for those counterparties for whom a person has already obtained U.S. person-related representations under the Guidance, U.S. person-related representations under the Final Rule will only be required from those counterparties with whom swaps are entered after December 31, 2027.

In response to commenters, the Commission has determined to add rule text permitting reliance on representations obtained under the Guidance.[172] The Commission understands that while the Guidance is non-binding, many market participants have chosen to develop policies and practices that take into account the views expressed therein, including expending time and resources to classify counterparties in accordance with the interpretation of the term ''U.S. person''

[164] *See* CFTC Staff Letter 18–13. *See also* CFTC Staff Letter 17–59 (Nov. 17, 2017) (providing no-action relief to NADB from the swap clearing requirement of section 2(h)(1) of the CEA), available at *https://www.cftc.gov/idc/groups/public/%40lrlettergeneral/documents/letter/17-59.pdf.*

[165] Proposed Rule, 85 FR at 962.

[166] Final § 23.23(a).

[167] Proposed § 23.23(a)(22)(iv); Proposed Rule, 85 FR at 962, 1003.

[168] Proposed Rule, 85 FR at 962.

[169] Final § 23.23(a)(23)(iv).

[170] Final § 23.23(a)(23)(iv)(A).

[171] Proposed Rule, 85 FR at 962.

[172] Final § 23.23(a)(23)(iv)(B).

as set forth in the Guidance. Adding rule text permitting reliance on representations obtained under the Guidance recognizes, and should reduce, the practical burdens of compliance with the Final Rule by enhancing regulatory certainty.

Finally, the rule text of § 23.23(a)(23)(iv)(B) clarifies that reliance is only permitted for representations obtained prior to the effective date of the Final Rule. As with U.S. person-related representations obtained pursuant to the Cross-Border Margin Rule, persons should not be permitted to rely on representations obtained pursuant to the Guidance after the effective date of the Final Rule when such persons could have also obtained representations pursuant to the Final Rule contemporaneously therewith.

6. Other

The Commission considers the following comments in connection with the proposed ''U.S. person'' definition beyond the scope of this rulemaking and is not addressing them in the Final Rule. However, the Commission takes these comments under advisement for any relevant future Commission action.

AIMA encouraged the CFTC to use the proposed ''U.S. person'' definition universally across all Title VII requirements and the CEA, including in part 4 for CPOs, commodity pools, and commodity trading advisors (''CTAs''). CS encouraged further harmonization of the ''U.S. person'' definition, to the extent possible, within the context of SD activity, including the CFTC's capital and margin rules. IIB/SIFMA recommended making conforming changes to the ''U.S. person'' definition under the Cross-Border Margin Rule to avoid the confusion that will arise from using different definitions of the same term in a single, comprehensive regulatory regime. Finally, JFMC/IBAJ and JSCC requested that the Commission specify that the ''U.S. person'' definition would also apply to, and supersede, the definition referenced in the CFTC's Orders of Exemption from Registration granted to the Japan Securities Clearing Corporation.[173]

C. Guarantee

1. Proposed Rule

The Commission proposed defining ''guarantee'' as an arrangement, pursuant to which one party to a swap has rights of recourse against a guarantor, with respect to its counterparty's obligations under the swap.[174] For these purposes, a party to a swap would have rights of recourse against a guarantor if the party has a conditional or unconditional legally enforceable right to receive or otherwise collect, in whole or in part, payments from the guarantor with respect to its counterparty's obligations under the swap. Also, the term ''guarantee'' would encompass any arrangement pursuant to which the guarantor itself has a conditional or unconditional legally enforceable right to receive or otherwise collect, in whole or in part, payments from any other guarantor with respect to the counterparty's obligations under the swap.

2. Summary of Comments

In general, AFEX/GPS, Chatham, IIB/SIFMA, and JFMC/IBAJ supported the proposed ''guarantee'' definition, while AFR, Barnard, and Better Markets opposed the proposed definition.

AFEX/GPS, Chatham, and JFMC/IBAJ supported the consistency of the proposed definition with the definition in the Cross-Border Margin Rule. JFMC/IBAJ also supported the consistency with the SEC Cross-Border Rule. AFEX/GPS and Chatham noted that the consistency would make the definition more workable.

AFEX/GPS stated that using the broad and vague definition of guarantee in the Guidance, which includes consideration of ''facts and circumstances'' and a non-exclusive list of examples, would not be appropriate, while the proposed definition would be objective and should facilitate compliance without sacrificing concerns about systemic risk flowing back to the United States. Chatham stated that the proposed definition would provide greater legal certainty around what is considered to be a guarantee and focuses the Commission's authority on potential significant risks to the U.S. financial system. IIB/SIFMA noted that the proposed definition would promote legal certainty by establishing a clearer test for when a non-U.S. person is considered to have financial support from a U.S. person, eliminating coverage of certain risk-shifting arrangements (*e.g.,* keepwells and liquidity puts) that do not provide a non-U.S. person's counterparty with recourse against a U.S. guarantor. IIB/SIFMA added that to the extent a firm uses the unlimited U.S. responsibility structure (discussed in section II.B.2.iv above), the Commission could sufficiently address the resulting risks to the United States by treating the firm as having a guarantee from a U.S. person, as the SEC does, rather than considering such an entity a U.S. person. JFMC/IBAJ stated that the definition under the Guidance introduced compliance challenges to market participants globally, including difficulties in confirming or obtaining representations from counterparties regarding whether certain arrangements, particularly purely internal arrangements within a counterparty's corporate group, constituted a ''guarantee.'' JFMC/IBAJ also supported the clarification that a non-U.S. person would be considered a ''guaranteed entity,'' as described below, only with respect to swaps that are guaranteed by a U.S. person.

ISDA, IIB/SIFMA, JFMC/IBAJ, and State Street also recommended that the Commission permit reliance on guarantee-related representations received pursuant to the Cross-Border Margin Rule and Guidance, analogous to the Proposed Rule and related comments with respect to the ''U.S. person'' definition, discussed above. IIB/SIFMA and State Street stated that such reliance should not be time limited.

AFR asserted that the narrower definition of guarantee, as compared to the Guidance, would permit numerous informal or even formal forms of guarantees between U.S. parent corporations and their subsidiaries to escape the definition. Barnard stated that the narrower definition would allow significant risk to be transferred back to the U.S. financial system over time. Barnard noted that economic implications are just as important as legal considerations, as confirmed and intended by CEA section 2(i)(1). Similarly, Better Markets recommended that the Commission revise its proposed definition of ''guarantee'' to include all forms of U.S. financial support used to facilitate dealing through non-U.S. affiliates because financial arrangements posing potential risks to U.S. persons and the U.S. financial system include more than solely contractual guarantees contained in swap trading relationship documentation between non-U.S. counterparties.

Better Markets added that a narrower definition of ''guarantee'' would elevate form over substance and have possible significant adverse effects on the U.S. financial system. Better Markets did not agree that a definition posing possible significant adverse effects on the U.S. financial system nevertheless should be adopted, merely because the proposed ''guarantee'' definition mirrors the definition in the Cross-Border Margin

[173] *See* Amended Order of Exemption from Registration issued for JSCC (May 15, 2017), available at *https://www.cftc.gov/idc/groups/public/@otherif/documents/ifdocs/jsccdcoexemptamdorder5-15-17.pdf.*

[174] Proposed § 23.23(a)(8); Proposed Rule, 85 FR at 963–64, 1002–03.

Rule and therefore would not demand ''a separate independent assessment.'' Better Markets asserted that it is neither a valid statutory purpose nor a benefit that outweighs, or even reasonably approximates, its costs. Better Markets added that CEA section 5(b) and related provisions make clear that the CFTC's core statutory policy objectives are to protect the safety and soundness of SDs, prevent disruptions to the integrity of derivatives markets, ensure the financial integrity of swaps transactions and the avoidance of systemic risk, and preserve the stability of the U.S. financial system.

Better Markets also stated that the CFTC's use of the margin-related ''guarantee'' definition is not appropriate. Its view was that margin requirements on uncleared swaps are market and credit risk mitigants that are imposed on specific portfolios of derivatives with specific counterparties, while the proposed definition would address broader systemic risk reduction and other policy objectives, including statutory concerns about the evasion of U.S. law through legal entity booking strategies. Further, Better Markets asserted that the narrower definition would increase risks to U.S. persons, because the definition would result in fewer swaps transactions being treated as ''guaranteed,'' opening a loophole for dealing conducted through unregistered affiliates of U.S. banks that nevertheless benefit from direct U.S. financial support.

3. Final Rule

After carefully considering the comments received, the Commission is adopting the definition of ''guarantee'' as proposed, with certain modifications and clarifications as discussed below.[175]

Consistent with the Cross-Border Margin Rule, the term ''guarantee'' applies regardless of whether the right of recourse is conditioned upon the non-U.S. person's insolvency or failure to meet its obligations under the relevant swap, and regardless of whether the counterparty seeking to enforce the guarantee is required to make a demand for payment or performance from the non-U.S. person before proceeding against the U.S. guarantor.[176] The terms of the guarantee need not necessarily be included within the swap documentation or even otherwise reduced to writing, provided that, under the laws of the relevant jurisdiction, a swap counterparty has a conditional or unconditional legally enforceable right, in whole or in part, to receive payments from, or otherwise collect from, the U.S. person in connection with the non-U.S. person's obligations under the swap. For purposes of the Final Rule, the Commission generally considers swap activities involving guarantees from U.S. persons to satisfy the ''direct and significant'' test under CEA section 2(i).[177]

However, in contrast to the Cross-Border Margin Rule and the Proposed Rule, but consistent with the recommendation by IIB/SIFMA, the Commission is interpreting ''guarantee'' in a manner similar to the SEC, specifically with respect to the unlimited U.S. responsibility prong. Similar to the SEC, when a non-U.S. person's counterparty has recourse to a U.S. person for the performance of the non-U.S. person's obligations under a swap by virtue of the U.S. person's unlimited responsibility for the non-U.S. person, such an arrangement is considered a guarantee, and as discussed in sections III.B.3.i and IV.B.3.i below, the non-U.S. person is required to include the swap in its SD and MSP threshold calculations, respectively.[178] As noted above, the Commission is not including the unlimited U.S. responsibility prong in the ''U.S. person'' definition, but interprets such relationships as guarantees to ensure they are appropriately covered by the Final Rule.

The term ''guarantee'' also encompasses any arrangement pursuant to which the counterparty to the swap has rights of recourse, regardless of the form of the arrangement, against at least one U.S. person (either individually, jointly, and/or severally with others) for the non-U.S. person's obligations under the swap. This addresses concerns that swaps could be structured such that they would not count toward a non-U.S. person's threshold calculations. For example, consider a swap between two non-U.S. persons (''Party A'' and ''Party B''), where Party B's obligations to Party A under the swap are guaranteed by a non-U.S. affiliate (''Party C''), and where Party C's obligations under the guarantee are further guaranteed by a U.S. parent entity (''Parent D''). The definition of ''guarantee'' deems a guarantee to exist between Party B and Parent D with respect to Party B's obligations under the swap with Party A.[179]

The Commission's definition of guarantee is not affected by whether the U.S. guarantor is an affiliate of the non-U.S. person because, regardless of affiliation, the swap counterparty has a conditional or unconditional legally enforceable right, in whole or in part, to receive payments from, or otherwise collect from, the U.S. person in connection with the non-U.S. person's obligations.

Also, the ''guarantee'' definition does not apply when a non-U.S. person has a right to be compensated by a U.S. person with respect to the non-U.S. person's own obligations under the swap. For example, consider a swap between two non-U.S. persons (''Party E'' and ''Party F''), where Party E enters into a back-to-back swap with a U.S. person (''Party G''), or enters into an agreement with Party G to be compensated for any payments made by Party E under the swap in return for passing along any payments received. In such an arrangement, a guarantee does not exist because Party F does not have a right to collect payments from Party G with respect to Party E's obligations under the swap (assuming no other agreements exist).[180]

As with the Cross-Border Margin Rule, the definition of ''guarantee'' in the Final Rule is narrower in scope than the one used in the Guidance.[181] Under the Guidance, the Commission advised that it would interpret the term ''guarantee'' generally to include not only traditional guarantees of payment or performance of the related swaps, but also other formal arrangements that, in view of all the facts and circumstances, support the non-U.S. person's ability to pay or perform its swap obligations. The Commission stated that it believed that it was necessary to interpret the term ''guarantee'' to include the different financial arrangements and structures that transfer risk directly back to the United States.[182] The Commission is aware that many other types of financial arrangements or support, other than a guarantee as defined in the Final Rule, may be provided by a U.S. person to a non-U.S. person (*e.g.,* keepwells and liquidity puts, certain types of indemnity agreements, master trust agreements, liability or loss transfer or sharing agreements). The Commission understands that these other financial arrangements or support transfer risk directly back to the U.S. financial system, with possible adverse effects, in a manner similar to a guarantee with a

[175] Final § 23.23(a)(9).

[176] Proposed Rule, 85 FR at 963–64. *See* 17 CFR 23.160(a)(2); Cross-Border Margin Rule, 81 FR at 34825.

[177] Proposed Rule, 85 FR at 963.

[178] *See* SEC Cross-Border Rule, 79 FR at 47316–47317, 47344.

[179] Proposed Rule, 85 FR at 963. *See* Cross-Border Margin Rule, 81 FR at 34825.

[180] Proposed Rule, 85 FR at 963. *See* Cross-Border Margin Rule, 81 FR at 34825.

[181] *See* Cross-Border Margin Rule, 81 FR at 34824.

[182] Guidance, 78 FR at 45320.

direct recourse to a U.S. person. However, the Commission has determined that a narrower definition of guarantee than that in the Guidance achieves a more workable framework for non-U.S. persons, particularly because the Final Rule's definition of ''guarantee'' is consistent with the Cross-Border Margin Rule, and therefore does not require a separate independent assessment, without undermining the protection of U.S. persons and the U.S. financial system. The Commission is sympathetic to comments regarding, and is independently aware of, the difficulty in confirming or obtaining representations from counterparties regarding whether certain arrangements, particularly purely internal arrangements within a counterparty's corporate group, constitute a ''guarantee.'' However, such difficulty does not extend to classifying as guarantees arrangements that provide a non-U.S. person's counterparty with recourse to a U.S. person for the performance of the non-U.S. person's obligations under a swap.

A broad definition of guarantee, as recommended by AFR, Barnard, and Better Markets, would make it difficult for certain entities to determine whether their counterparty is guaranteed or not. General consistency with the Cross-Border Margin Rule definition means no additional burden for market participants. Additionally, though the definition of ''guarantee'' in the Guidance was broader, having a specific standard in a rule is preferable to an open-ended interpretation. The Commission recognizes that the definition of ''guarantee'' could lead to certain entities counting fewer swaps towards their SD or MSP thresholds or qualify additional counterparties for exceptions to certain regulatory requirements as compared to the definition in the Guidance. However, such concerns could be mitigated to the extent such non-U.S. persons meet the definition of a ''significant risk subsidiary,'' and thus, as discussed below, are required to count certain swaps or swap positions toward their SD or MSP registration thresholds. In this way, non-U.S. persons receiving support from a U.S. person and representing a significant risk to the U.S. financial system are captured by the Final Rule. Accordingly, the Final Rule achieves the dual goals of protecting the U.S. markets and promoting a workable cross-border framework.

In response to comments, the Commission is adopting language in the ''guarantee'' definition that is parallel to the language for ''U.S. persons,'' allowing persons to rely on counterparty representations with respect to a counterparty's ''guarantee'' status obtained pursuant to the Cross-Border Margin Rule. As discussed above, permitting temporary reliance to facilitate this method of updating representations is less burdensome and more cost efficient than requiring all affected SDs to update representations within a relatively brief compliance period. However, permanent reliance on representations obtained under the Guidance or the Cross-Border Margin Rule would be inconsistent with good recordkeeping practices, particularly for dormant relationships, thus, the Commission has determined to require an updated representation within a set time period. The Commission is thus adopting an approximately seven year time limit, until December 31, 2027, on counterparty representations with respect to a counterparty's ''guarantee'' status obtained pursuant to the Cross-Border Margin Rule, the same as is permitted for reliance on the ''U.S. person'' representations. Thus, for those counterparties for whom a person has already obtained guarantee-related representations under the Cross-Border Margin Rule, guarantee-related representations under the Final Rule will only be required from those counterparties with whom swaps are entered after December 31, 2027. Nevertheless, best practice is to obtain updated representations as soon as practicable.

In addition, the Commission has adjusted the rule text of § 23.23(a)(9) to clarify that reliance is only permitted for representations obtained prior to the effective date of the Final Rule.[183] Persons should not be permitted to rely on representations obtained pursuant to the Cross-Border Margin Rule after the effective date of the Final Rule when such persons could have also obtained representations pursuant to the Final Rule contemporaneously therewith.

The Commission believes that any ''guarantee'' related representation received under the Guidance definition would also apply under the Final Rule, as the Final Rule's definition is generally narrower in scope. Therefore, the Commission is of the view that market participants may also rely on representations previously obtained using the ''guarantee'' definition in the Guidance.[184] Nevertheless, a representation obtained under the Guidance should not be relied on permanently and should be obtained as soon as practicable, but in the Commission's view it would not be appropriate to rely on representations under the Guidance after the December 31, 2027 deadline for similar representations made under the Cross-Border Margin Rule. Thus, for those counterparties for whom a person has already obtained guarantee-related representations under the Guidance, guarantee-related representations under the Final Rule will only be required from those counterparties with whom swaps are entered after December 31, 2027.

In response to commenters, the Commission has determined to add rule text permitting reliance on representations obtained under the Guidance.[185] The Commission understands that while the Guidance is non-binding, many market participants have chosen to develop policies and practices that take into account the views expressed therein, including expending time and resources to classify counterparties in accordance with the interpretation of the term ''guarantee'' as set forth in the Guidance. Adding rule text permitting reliance on representations obtained under the Guidance recognizes, and should reduce, the practical burdens of compliance with the Final Rule by enhancing regulatory certainty.

Finally, the rule text of § 23.23(a)(9)(ii) clarifies that reliance is only permitted for representations obtained prior to the effective date of the Final Rule. As with guarantee-related representations obtained pursuant to the Cross-Border Margin Rule, persons should not be permitted to rely on representations obtained pursuant to the Guidance after the effective date of the Final Rule when such persons could have also obtained representations pursuant to the Final Rule contemporaneously therewith.

For ease of understanding, the discussion in this release uses the term ''Guaranteed Entity'' to refer to a non-U.S. person whose swaps are guaranteed by a U.S. person, but only with respect to the swaps that are so guaranteed. Thus, a non-U.S. person may be a Guaranteed Entity with respect to its swaps with certain counterparties because the non-U.S. person's swaps with those counterparties are guaranteed, but would not be a Guaranteed Entity with respect to its

183 Final § 23.23(a)(9)(i).

184 An SD or MSP may not rely on a representation obtained for purposes of the Guidance that a counterparty's swaps are not guaranteed by a U.S. person if the SD or MSP has classified the counterparty as a U.S. person under the unlimited U.S. responsibility prong of the U.S. person definition in the Guidance.

185 Final § 23.23(a)(9)(ii).

swaps with other counterparties if the non-U.S. person's swaps with the other counterparties are not guaranteed by a U.S. person. In other words, depending on the nature of the trading relationship, a single entity could be a Guaranteed Entity with respect to some of its swaps, but not others.

Additionally, this release uses the term ''Other Non-U.S. Person'' to refer to a non-U.S. person that is neither a Guaranteed Entity nor a significant risk subsidiary (as defined below).[186] Depending on an entity's corporate structure and financial relationships, a single entity could be both a Guaranteed Entity and a significant risk subsidiary and, as noted above, it may be a Guaranteed Entity for certain of its swaps and an Other Non-U.S. Person for others.

D. Significant Risk Subsidiary, Significant Subsidiary, Subsidiary, Parent Entity, and U.S. GAAP

1. Proposed Rule

The Commission proposed a new category of entity termed a significant risk subsidiary (''SRS''). Under the Proposed Rule, a non-U.S. person would be considered an SRS if: (1) The non-U.S. person is a ''significant subsidiary'' of an ''ultimate U.S. parent entity,'' as those terms were proposed to be defined; (2) the ''ultimate U.S. parent entity'' has more than $50 billion in global consolidated assets, as determined in accordance with U.S. generally accepted accounting principles (''GAAP'') at the end of the most recently completed fiscal year; and (3) the non-U.S. person is not subject to either: (a) Consolidated supervision and regulation by the Board of Governors of the Federal Reserve System (''Federal Reserve Board'') as a subsidiary of a U.S. bank holding company (''BHC''); or (b) capital standards and oversight by the non-U.S. person's home country regulator that are consistent with the Basel Committee on Banking Supervision's ''International Regulatory Framework for Banks'' (''Basel III'') and margin requirements for uncleared swaps in a jurisdiction for which the Commission has issued a comparability determination (''CFTC Margin Determination'') with respect to uncleared swap margin requirements.[187] If an entity is determined to be an SRS, the Commission proposed to apply certain regulations to the entity in the same manner as a U.S. person in some instances, for example in the application of the SD and MSP registration threshold calculations, and in the same manner as a Guaranteed Entity in other instances, for example in the application of group B and C requirements.

With respect to conduit affiliates, the Guidance included a discussion of factors that would be taken into account when determining whether an entity was a conduit affiliate of a U.S. person. The Proposed Rule stated that this concept was not being included in the proposed regulations because the concerns posed by a conduit affiliate were intended to be addressed through the proposed definition and regulation of SRSs.

2. Summary of Comments

In the Proposed Rule, the Commission asked whether it should use the concept of a conduit affiliate, as was done in the Guidance, in order to harmonize with the SEC.[188] AEFX/GPS, Chatham, JFMC/IBAJ, and IIB/SIFMA all stated that they prefer the SRS entity definition to the use of the conduit affiliate concept from the Guidance. AFEX/GPS, Chatham, and IIB/SIFMA stated that the objective criteria in the SRS definition are preferable to the conduit affiliate concept in the Guidance, which is more difficult to apply. JFMC/IBAJ and IIB/SIFMA also commented that the SRS definition is an improvement over the FCS concept previously proposed in the 2016 Proposal because the SRS definition excludes those subsidiaries that are not significant to their parent entities. Better Markets stated that the proposed SRS definition does not address the avoidance and evasion risks addressed by the conduit affiliate concept in the Guidance. IATP suggested that the previously proposed FCS concept be retained in place of the SRS definition. JBA stated that market participants have already assessed, under the Guidance, whether their activities are subject to the swap rules based on the attributes of their counterparties and requiring them to re-assess will create significant burdens on market participants. ISDA suggested that with respect to SRSs, entities should be permitted to rely on counterparty representations pertaining to conduit affiliates as described in the Guidance.

CS and IIB/SIFMA stated that the exclusion for subsidiaries of BHCs in the SRS definition should be expanded to include those entities that are subsidiaries of intermediate holding companies (''IHCs''). These commenters noted that IHCs are subject to prudential regulation, including Basel III capital requirements, stress testing, liquidity, and risk management requirements.

JFMC/IBAJ and IIB/SIFMA suggested that accounting consolidation does not create a sufficient jurisdictional nexus to the United States because there is no requirement that the U.S. entity be directly liable for the foreign subsidiary's swaps. These commenters stated that if the SRS definition is nevertheless retained then the proposed significance tests should also be retained. IIB/SIFMA and the Working Group stated that the definition of ultimate U.S. parent entity should be limited to those groups of entities where the top-tier ultimate parent company is a U.S. person.

With respect to the exception in § 23.23(a)(13)(i) for subsidiaries of BHCs, AFR and Better Markets stated that the Commission should eliminate this exception because deference to the prudential regulators in this way is not justified. AFR noted the failure of prudential supervision of banks to adequately address derivatives markets risks prior to the 2008 financial crisis. IATP, AFR, and Barnard stated that the broad exemptions would exclude almost all foreign subsidiaries of U.S. companies and be a significant reduction in the application of the Commission's swap regulations. Better Markets stated that the Commission does not have the discretion to determine whether and when to apply U.S. regulatory requirements based on principles of international comity when there is a direct and significant risk to U.S. BHCs and the U.S. financial system.

Better Markets suggested that if the SRS definition is retained then there should be two additional significance tests added to those in § 23.23(a)(14). This commenter proposed that if an entity were to meet a risk transfer test, measuring the notional amount of swaps that are back-to-backed with U.S. entities, or a risk acceptance test, measuring the trading activity of the subsidiary over a three month time period, then the entity would be considered a significant subsidiary.

The Working Group suggested that the proposed SRS definition should be modified to limit the applicability to only those entities that qualify as financial entities because the systemic risk associated with non-financial entities is mitigated because their activities primarily take place outside of the financial system. The Working Group agreed with the Commission's proposal to exclude from the SRS definition those entities that are subject to oversight by the non-U.S. person's home country regulator and capital

[186] Note that an Other Non-U.S. Person can include a registered SD or MSP.

[187] Proposed Rule, 85 FR at 964–968.

[188] Proposed Rule, 85 FR at 969–970.

standards consistent with Basel III. However, the commenter added that to the extent a regulator has exempted a particular type of entity from capital requirements otherwise consistent with Basel III, the CFTC should defer to such exemption and consider such entity as subject to comparable capital requirements.

3. Final Rule and Commission Response

The Commission is adopting the SRS definition as proposed, with two modifications as discussed below. First, the Final Rule adds IHCs to the exclusion in § 23.23(a)(13)(i) for those companies that are subject to consolidated supervision and regulation by the Federal Reserve Board. Second, with respect to the carve-out in § 23.23(a)(13)(ii), the Final Rule makes a clarifying revision to the margin requirements aspect of that provision.

(i) Non-U.S. Persons With U.S. Parent Entities

As discussed in the Proposed Rule, in addition to the U.S. persons described above in section II.B, the Commission understands that U.S. persons may organize the operations of their businesses through the use of one or more subsidiaries that are organized and operated outside the United States.[189] Through consolidation, non-U.S. subsidiaries of U.S. persons may permit U.S. persons to accrue risk through the swap activities of their non-U.S. subsidiaries. This risk, in the aggregate, may have a significant effect on the U.S. financial system. Therefore, the Commission may subject consolidated non-U.S. subsidiaries of U.S. persons to Commission regulation due to their direct and significant relationship to their U.S. parent entities. Further, consolidated non-U.S. subsidiaries of U.S. parent entities present a greater supervisory interest to the CFTC, relative to Other Non-U.S. Persons.[190] Moreover, because U.S. persons have regulatory obligations under the CEA that Other Non-U.S. Persons may not have, consolidated non-U.S. subsidiaries of U.S. parent entities present a greater supervisory interest to the CFTC relative to Other Non-U.S. Persons due to the Commission's interest in preventing the evasion of obligations under the CEA.

Pursuant to the consolidation requirements of U.S. GAAP, the financial statements of a U.S. parent entity reflect the financial position and results of operations of that parent entity, together with the network of branches and subsidiaries in which the U.S. parent entity has a controlling interest, including non-U.S. subsidiaries, which is an indication of connection and potential risk to the U.S. parent entity. Consolidation under U.S. GAAP is predicated on the financial control of the reporting entity. Therefore, an entity within a financial group that is consolidated with its parent entity for accounting purposes in accordance with U.S. GAAP is subject to the financial control of that parent entity. By virtue of consolidation then, a non-U.S. subsidiary's swap activity creates direct risk to the U.S. parent.[191] That is, as a result of consolidation and financial control, the financial position, operating results, and statement of cash flows of a non-U.S. subsidiary are included in the financial statements of its U.S. parent and therefore affect the financial condition, risk profile, and market value of the parent. Because of that relationship, risks taken by a non-U.S. subsidiary can have a direct effect on the U.S. parent entity. Furthermore, a non-U.S. subsidiary's counterparties may generally look to both the subsidiary and its U.S. parent for fulfillment of the subsidiary's obligations under a swap, even without any explicit guarantee. In many cases, counterparties would not enter into the transaction with the subsidiary (or would not do so on the same terms), and the subsidiary would not be able to engage in a swap business, absent this close relationship with a parent entity. In addition, a non-U.S. subsidiary may enter into offsetting swaps or other arrangements with its U.S. parent entity or other affiliate(s) to transfer the risks and benefits of swaps with non-U.S. persons to its U.S. affiliates, which could also lead to risk for the U.S. parent entity. Because such swap activities may have a direct effect on the financial position, risk profile, and market value of a U.S. parent entity, they can lead to spill-over effects on the U.S. financial system.

IIB/SIFMA and JFMC/IBAJ stated that there is no legal basis to apply swap regulations based on accounting consolidation. The Commission continues to believe, as it stated in its Cross-Border Margin Rule, by virtue of an entity having its financial statements consolidated with those of its U.S. ultimate parent, the financial position, operating results, and statement of cash flows of the entity are included in the financial statements of its U.S. ultimate parent entity and therefore affect the financial position, risk profile, and market value of the U.S. ultimate parent. Because of the entity's direct relationship with, and the possible negative effect of its swap activities on, its U.S. ultimate parent entity and the U.S. financial system, the entity raises greater supervisory concern in the United States relative to other non-U.S. swap entities.[192] Accordingly, it is appropriate to apply certain swap regulations to certain entities that have financial statements consolidated with U.S. parent entities.

However, the principles of international comity militate against applying the Commission's swap regulations to all non-U.S. subsidiaries of U.S. parent entities. Rather, it is consistent with such principles to apply a risk-based approach to determining which of such entities should be required to comply with the Commission's swap requirements. The Commission's approach in the Final Rule, as discussed further below with respect to the exclusion for subsidiaries of BHCs and IHCs, makes that determination in a manner that accounts for the risk that non-U.S. subsidiaries may pose to the U.S. financial system and the ability of large global entities to operate efficiently outside the United States. The Commission's risk-based approach is embodied in the definition of an SRS, which, as discussed above, captures entities whose obligations under swaps may not be guaranteed by U.S. persons, but nonetheless raise particular supervisory concerns in the United States due to the possible negative effect on their ultimate U.S. parent entities and thus the U.S. financial system.

(ii) Preliminary Definitions

For purposes of the SRS definition, the term ''subsidiary'' means an affiliate of a person controlled by such person directly, or indirectly through one or more intermediaries.[193] The definition of ''subsidiary'' has been revised in the Final Rule for clarity. For purposes of this definition, an affiliate of, or a person affiliated with, a specific person is a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.[194] In the Final Rule, the definition of ''affiliate'' has been moved out of the definition of ''subsidiary'' and into its own definition for added clarity, since the term ''affiliate'' is relevant for other provisions of the Final Rule, as

[189] Proposed Rule, 85 FR at 964.

[190] This release uses the term ''Other Non-U.S. Person'' to refer to a non-U.S. person that is neither a Guaranteed Entity nor an SRS.

[191] Proposed Rule, 85 FR at 964.

[192] *See* Cross-Border Margin Rule, 81 FR at 34827.

[193] Final § 23.23(a)(15).

[194] Final § 23.23(a)(1).

discussed in this release. The term ''control,'' including controlling, controlled by, and under common control with, means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting shares, by contract, or otherwise.[195] The definition of ''control'' is also relevant to other provisions of the Final Rule, as discussed in this release. The definitions of subsidiary, affiliate, and control are substantially similar to the definitions found in SEC Regulation S–X.[196] Further, under the Final Rule, the term ''parent entity'' means any entity in a consolidated group that has one or more subsidiaries in which the entity has a controlling interest, in accordance with U.S. GAAP.[197] U.S. GAAP is defined in the Final Rule as U.S. generally accepted accounting principles.[198]

Notably, a U.S. parent entity for purposes of the definition of SRS need not be a non-U.S. subsidiary's ultimate parent entity. The SRS definition encompasses U.S. parent entities that may be intermediate entities in a consolidated corporate family with an ultimate parent entity located outside the U.S. To differentiate between multiple possible U.S. parent entities, the Final Rule defines an ''ultimate U.S. parent entity'' for purposes of the significant subsidiary test. A non-U.S. person's ''ultimate U.S. parent entity'' is the U.S. parent entity that is not a subsidiary of any other U.S. parent entity.[199] Risk of a non-U.S. subsidiary that flows to its U.S. parent entity may not flow back out of the U.S. to a non-U.S. ultimate or intermediate parent entity. Because the risk may ultimately stop in the United States, the Commission is basing the SRS definition on whether a non-U.S. person has any U.S. parent entity, subject to certain risk-based thresholds.

IIB/SIFMA and the Working Group stated that the SRS definition should be limited to subsidiaries that have a ''top-tier'' U.S. person parent entity, rather than including subsidiaries that have a U.S. parent entity that may not be the ultimate parent entity. The Commission is including subsidiaries that have non-''top-tier'' U.S. parent entities because the risk that the subsidiary poses may be consolidated in the United States. The Final Rule treats all subsidiaries of U.S. parent entities equally, regardless of where the U.S. parent entity sits in the corporate structure.

(iii) Significant Risk Subsidiaries

In addition to the definitions discussed above, whether an entity is an SRS depends on the size of its ultimate U.S. parent entity, the significance of the subsidiary to its ultimate U.S. parent entity, and the regulatory oversight of its ultimate U.S. parent entity or the regulatory oversight of the non-U.S. subsidiary in the jurisdiction in which it is regulated.

Under the Final Rule, the ultimate U.S. parent entity must exceed a $50 billion consolidated asset threshold.[200] The Commission is adopting the $50 billion threshold after considering both the Commission's interest in adequately overseeing those non-U.S. persons that may have a significant effect on their ultimate U.S. parent entity—and, by extension—the U.S. financial system, and also its interest in avoiding unnecessary burdens on those non-U.S. persons that would not have such an effect.[201] The $50 billion threshold limits the burden of the SRS definition to only those entities whose ultimate U.S. parent entity may pose a systemic risk to the U.S. financial system.

In addition, before a non-U.S. subsidiary of an ultimate U.S. parent entity that meets the $50 billion consolidated asset threshold is an SRS, the subsidiary needs to constitute a significant part of its ultimate U.S. parent entity. This concept of a ''significant subsidiary'' borrows from the SEC's definition of ''significant subsidiary'' in Regulation S–X, as well as the Federal Reserve Board in its financial statement filing requirements for foreign subsidiaries of U.S. banking organizations.[202] The Commission is focusing on only those subsidiaries that are significant to their ultimate U.S. parent entities, in order to capture those subsidiaries that have a significant effect on their large ultimate U.S. parent entities. To provide certainty to market participants as to what constitutes a significant subsidiary, the Final Rule includes a set of quantitative significance tests. Although not identical, the SEC includes similar revenue and asset significance tests in its definition of significant subsidiary in Regulation S–X.[203] In this case, in order to determine whether a subsidiary meets such significance, the Final Rule measures the significance of a subsidiary's equity capital, revenue, and assets relative to its ultimate U.S. parent entity.

Under the Final Rule, the term ''significant subsidiary'' means a subsidiary, including its own subsidiaries, where: (1) The three year rolling average of the subsidiary's equity capital is equal to or greater than five percent of the three year rolling average of its ultimate U.S. parent entity's consolidated equity capital, as determined in accordance with U.S. GAAP at the end of the most recently completed fiscal year (the ''equity capital significance test''); (2) the three year rolling average of the subsidiary's revenue is equal to or greater than ten percent of the three year rolling average of its ultimate U.S. parent entity's consolidated revenue, as determined in accordance with U.S. GAAP at the end of the most recently completed fiscal year (the ''revenue significance test''); or (3) the three year rolling average of the subsidiary's assets is equal to or greater than ten percent of the three year rolling average of its ultimate U.S. parent entity's consolidated assets, as determined in accordance with U.S. GAAP at the end of the most recently completed fiscal year (the ''asset significance test'').[204] For the equity capital significance test, equity capital includes perpetual preferred stock, common stock, capital surplus, retained earnings, accumulated other comprehensive income, and other equity capital components and is calculated in accordance with U.S. GAAP.

The Final Rule results in an entity being a significant subsidiary only if it passes at least one of these significance tests. The equity capital test is used to measure a subsidiary's significance to its ultimate U.S. parent entity and is used in the context of financial statement reporting of foreign subsidiaries.[205] If a subsidiary constitutes more than ten percent of its ultimate U.S. parent entity's assets or revenues, it is of significant importance to its ultimate U.S. parent entity such that swap activity by the subsidiary may

[195] Final § 23.23(a)(2).

[196] *See* 17 CFR 210.1–02. Regulation S–X generally covers the form and content requirements for financial statements.

[197] Final § 23.23(a)(12).

[198] Final § 23.23(a)(22).

[199] Final § 23.23(a)(19).

[200] Final § 23.23(a)(13).

[201] Proposed Rule, 85 FR at 965.

[202] *See e.g.,* Instructions for Preparation of Financial Statements of Foreign Subsidiaries of U.S. Banking Organizations FR 2314 and FR 2314S, at GEN–2 (Sept. 2016), available at *https://www.federalreserve.gov/reportforms/forms/FR_2314--FR_2314S20190331_i.pdf* (''FR 2314 and FR 2314S Instructions'') (identifying equity capital significance test applicable to subsidiaries). *See also* SEC rule 210.1–02(w), 17 CFR 210.1–02(w) (identifying asset and income significance tests applicable in definition of significant subsidiaries).

[203] 17 CFR 210.1–02(w)(1)–(3) (setting out a ten percent significance threshold with respect to total assets and income).

[204] Final § 23.23(a)(14).

[205] *See* FR 2314 and FR 2314S Instructions, at Gen-2.

have a material effect on its ultimate U.S. parent entity and, consequently, the U.S. financial system. The Commission is using a three year rolling average throughout its significance tests in order to mitigate the potential for frequent changes in an entity's SRS status based on fluctuations in its share of equity capital, revenue, or assets of its ultimate U.S. parent entity. If a subsidiary satisfies any one of the three significance tests, then it is of sufficient significance to its ultimate U.S. parent entity, which under § 23.23(a)(13) has consolidated assets of more than $50 billion, to warrant the application of requirements addressed by the Final Rule if such subsidiary otherwise meets the definition of SRS.

As noted above, Better Markets suggested that the Commission add two activity-based tests to the proposed significant subsidiary definition: A risk transfer test and a risk acceptance test. The Commission declines to include these two tests because they do not consider the risk to the broader financial system of the entities that are potentially captured by the Final Rule. Better Markets' proposed tests are activity-based, rather than risk-based, whereas the Commission has determined to apply swap requirements to foreign entities using a risk-based test. Better Markets' proposed tests would set thresholds above which an entity would be deemed to be significant subsidiaries, however these tests do not provide any measure that is relative to the parent entity. Such notional-based thresholds may be a measure of activity, but they are not a measure of risk that a subsidiary poses to a parent entity.[206] The significance tests adopted here to identify SRSs include those entities that meet the commenters' proposed tests to the extent those entities pose what the Commission considers a significant risk to the financial system.

(iv) Exclusions From the Definition of SRS

As indicated above, under the Final Rule, a non-U.S. person will not be an SRS to the extent the entity is subject to prudential regulation as a subsidiary of a U.S. BHC or IHC, or is subject to comparable capital and margin standards.[207] An entity that meets either of those two exceptions, in the Commission's view, is subject to a level of regulatory oversight that is sufficiently comparable to the Dodd-Frank Act swap regime with respect to prudential oversight. Non-U.S. subsidiaries that are part of BHCs are already subject to consolidated supervision and regulation by the Federal Reserve Board,[208] including with respect to capital and risk management requirements, and therefore their swap activity poses less risk to the financial position and risk profile of the ultimate U.S. parent entity, and thus less risk to the U.S. financial system than the swap activity of a non-U.S. subsidiary of an ultimate U.S. parent entity that is not a BHC.[209] In this case, deference to the foreign regulatory regime is appropriate because the swap activity is occurring within an organization that is under the umbrella of U.S. prudential regulation with certain regulatory protections already in place.

The exclusion from the SRS definition for subsidiaries of IHCs is being added to the Final Rule in response to comments. IHCs are subject to prudential standards of the Federal Reserve Board that are similar to those that apply to BHCs. In general, IHCs and BHCs of similar size are subject to similar liquidity, risk management, stress testing, and credit limit standards.[210] Therefore, for the same risk-based reasons that the Commission proposed to exclude subsidiaries of BHCs from the definition of SRS,[211] the Commission is expanding the SRS exclusion to include subsidiaries of both BHCs and IHCs in § 23.23(a)(13)(i).

In response to comments from AFR and Better Markets that the Commission should not defer to the prudential regulators with respect to the regulation of derivative market activity of BHCs and those entities subject to the required non-U.S. capital and margin regimes, under the Guidance, absent a guarantee, the Commission had generally not expected these entities to count their swaps or swap positions with non-US persons towards the SD or MSP thresholds or, if registered as swap entities, comply with Transaction-Level Requirements (discussed in section VI below) when transacting with non-U.S. persons that were not guaranteed by a U.S. person nor acting as conduit affiliates. Thus, the deference to U.S. and non-U.S. prudential regulators in the Final Rule maintains the status quo of the last seven years rather than representing a relinquishment of existing regulatory oversight by the Commission. Moreover, the SRS definition does not defer to prudential regulators to regulate derivatives market activity, which is carried on by the foreign subsidiary, but rather defers to the role of prudential regulation in the consolidated oversight of prudential risk in evaluating the extent to which the Commission should expand its oversight of non-U.S. entities that are not guaranteed by a U.S. person beyond the Guidance. For the reasons noted above, the Commission has determined not to apply the Final Rule on the basis of accounting consolidation alone, but rather, in exercising its oversight of non-U.S. entities, has taken a risk-based approach to determining which foreign subsidiaries present a significant risk to their ultimate U.S. parent and thus to the U.S. financial system. The Commission thus has determined that because the risk presented by foreign subsidiaries that are consolidated with a BHC or IHC, or are subject to the specified prudential regulation in their local jurisdiction, is already being adequately monitored, such foreign subsidiaries should not also be subject to the Commission's oversight.

With respect to the BHC exception, Better Markets suggested that the Commission does not have the legal discretion to defer to prudential regulators because of the requirements in CEA section 2(i). As the Commission stated in the Proposed Rule, CEA section 2(i) does not require the Commission to extend its reach to the outer bounds of the authorization provided in CEA section 2(i).[212] In determining how to exercise its authority, the Commission stated that it will be guided by principles of international comity and will focus its authority on potential significant risks to the U.S. financial system. The Commission noted that the Restatement also provides that even where a country has a basis for extraterritorial jurisdiction, it should not prescribe law with respect to a person or activity in another country when the exercise of

[206] The Commission also has noted in the past that such notional amount-based thresholds are not measures of the exposure or risk of particular swap positions. *See* Entities Rule, 77 FR at 30630.

[207] Final § 23.23(a)(13)(i)–(ii).

[208] *See e.g.,* Board of Governors of the Federal Reserve System, Bank Holding Company Supervision Manual, section 2100.0.1 Foreign Operations of U.S. Banking Organizations, available at *https://www.federalreserve.gov/publications/files/bhc.pdf* (''The Federal Reserve has broad discretionary powers to regulate the foreign activities of member banks and [BHCs] so that, in financing U.S. trade and investments abroad, these U.S. banking organizations can be competitive with institutions of the host country without compromising the safety and soundness of their U.S. operations.''); FR 2314 and FR 2314S Instructions, at GEN 2.

[209] Proposed Rule, 85 FR at 966.

[210] *See e.g.,* Prudential Standards for Large Bank Holding Companies, Savings and Loan Holding Companies, and Foreign Banking Organizations, 84 FR 59032 (Nov. 2019).

[211] Proposed Rule, 85 FR at 966.

[212] *Id.* at 955.

such jurisdiction is unreasonable.[213] In the context of the SRS definition, the risk-based approach to limiting the application of the Commission's requirements extraterritorially focuses its requirements on those entities that pose significant risk to the U.S. financial system, as discussed above.

Similarly, in the case of entities that are subject to capital standards and oversight by their home country regulators that are consistent with Basel III and subject to a CFTC Margin Determination, the Commission will defer to the home country regulator.[214] In cases where entities are subject to capital standards and oversight by home country regulators that are consistent with Basel III and subject to a CFTC Margin Determination, the potential risk that the entity might pose to the U.S. financial system is adequately addressed through these home country capital and margin requirements. Further, such an approach is consistent with the Commission's historical commitment to show deference to non-U.S. regulators whose requirements are comparable to the CFTC's requirements. To make clear that the CFTC Margin Determination must be a positive determination of comparability, the provision in § 23.23(a)(13)(ii) has been modified to read ''and margin requirements for uncleared swaps in a jurisdiction that the Commission has found comparable pursuant to a published comparability determination with respect to uncleared swap margin requirements.'' For margin purposes, the Commission has issued a number of determinations that entities can look to in order to determine if they satisfy this aspect of the exception.[215] For capital standards and oversight consistent with Basel III, entities should look to whether the BIS has determined the jurisdiction is in compliance as of the relevant Basel Committee on Banking Supervision deadline set forth in its most recent progress report.[216] The Commission is excluding these entities from the definition of SRS, in large part, because the swaps entered into by such entities are already subject to significant regulation, either by the Federal Reserve Board or by the entity's home country.

The Working Group suggested that where a jurisdiction has capital and margin requirements consistent with Basel III requirements, but certain entities located in that jurisdiction are exempted from those requirements, such entities should nonetheless be considered as subject to sufficient capital and margin requirements for the purpose of the proposed SRS exclusion. The Commission is declining to adopt this suggestion here, but it may warrant further consideration in the future. It is not clear whether a foreign jurisdiction's exemption from capital and margin requirements would be based on a risk assessment of the exempted entities, whether such exemptions are granted on a case-by-case basis or provided to entire classes or categories, or whether such exemptions are based on deference to some other form of prudential regulation. Under the Final Rule, where an entity is exempt from a country's capital and margin requirements, such an entity will not be considered to be subject to sufficient capital and margin requirements for the purpose of the SRS exclusion. As noted above, if a non-U.S. subsidiary of an ultimate U.S. parent entity does not fall into either of the exceptions in § 23.23(a)(13)(i) through (ii), the Final Rule classifies the subsidiary as a SRS only if its ultimate U.S. parent entity has more than $50 billion in global consolidated assets and if the subsidiary meets the definition of a significant subsidiary, set forth in § 23.23(a)(14).

With respect to the Working Group comment that the SRS definition should not apply to non-financial entities, the Commission has determined to apply the SRS definition to those non-financial entities that satisfy the risk-based tests contained in the definition. Those entities are not subject to prudential regulation and are, by definition, significant subsidiaries of large U.S. parent entities that may pose a risk to the U.S. financial system, and therefore the Commission believes that such entities should not be excluded from the SRS definition. Accordingly, the Commission is not adding an exception for non-financial entities to the SRS definition. However, Other Non-U.S. Person counterparties to SRSs are not required to include such swaps in either their SD or MSP registration threshold calculations, as discussed below. The Commission has also determined for the Final Rule that non-U.S. swap entities that are neither SRSs nor Guaranteed Entities are not required to comply with the group B and group C requirements (as defined in section VI.A.2 and VI.A.3 below) when entering into foreign-based swaps with certain foreign counterparties, including SRSs that are neither swap entities nor Guaranteed Entities (''SRS End Users'').[217] This application of the Final Rule should assuage the commenter's concerns about the effect SRS status will have on the swap trading relationships of a non-financial entity that is an SRS but does not engage in swap dealing or meet the definition of MSP.

In response to Better Markets' comment that the SRS definition does not address evasion and avoidance concerns that are addressed by the conduit affiliate concept, the Commission believes that the SRS definition adequately addresses those concerns within a risk-based framework. The Commission believes that to the extent an off-shore entity is entering into transactions with non-U.S. entities and subsequently back-to-backing those transactions to a U.S. entity, it is appropriate to subject such an entity to certain of the Commission's swap requirements if that entity meets the definition of an SRS and is consequently a significant subsidiary of a U.S. parent entity that is significant to the U.S. financial system. This approach is a risk-based assessment rather than merely a structural or activity-based assessment. Without this risk-based approach, the SD de minimis threshold, which is a strictly activity-based test (*i.e.,* a test based on the aggregate gross notional amount of dealing activity), becomes the de facto risk test of when an entity would be subject to the Commission's swap requirements as an SD. The Commission continues to believe that the risk-based SRS test is better-suited to make such a determination.

[213] *Id.* at 957.

[214] Final § 23.23(a)(13)(ii).

[215] *See* Comparability Determination for Japan: Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 81 FR 63376 (Sep. 15, 2016); Comparability Determination for the European Union: Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 82 FR 48394 (Oct. 13, 2017) (''Margin Comparability Determination for the European Union''); Amendment to Comparability Determination for Japan: Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 84 FR 12074 (Apr. 1, 2019); Comparability Determination for Australia: Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 84 FR 12908 (Apr. 3, 2019). Further, on April 5, 2019, DSIO and the Division of Market Oversight (''DMO'') issued a letter jointly to provide time-limited no-action relief in connection with, among other things, the Margin Comparability Determination for the European Union, in order to account for the anticipated withdrawal of the United Kingdom from the European Union. *See* CFTC Staff Letter 19–08, No-Action Relief in Connection With Certain Previously Granted Commission Determinations and Exemptions, in Order to Account for the Anticipated Withdrawal of the United Kingdom From the European Union (Apr. 5, 2019), available at *https://www.cftc.gov/csl/19-08/download.*

[216] The most current report was issued in July 2020. Basel Committee on Banking Supervision, Eighteenth progress report on adoption of the Basel regulatory framework (July 2020), available at *https://www.bis.org/bcbs/publ/d506.pdf.* Current and historical reports are available at *https://www.bis.org/bcbs/implementation/rcap_reports.htm?m=3%7C14%7C656%7C59.*

[217] *See infra* section VI.B.

(v) Counterparty Status and Representations

The Commission acknowledges comments that the implementation of the SRS definition may require entities to reevaluate the status of their counterparties. The Commission understands that SDs may have to re-document whether their counterparties are SRS entities and that this could require, for example, a new industry protocol, which may be an additional burden resulting from the adoption of this rule. The potential burden of this re-assessment of counterparties is considered in the cost-benefit considerations section of this adopting release.

Regarding the ISDA comment that the Commission should permit swap entities to rely on representations obtained under the Guidance with respect to the status of counterparties as conduit affiliates, the Commission responds that the representations made by counterparties with respect to the conduit affiliate concept in the Guidance are not applicable to the SRS definition. Because the definition of an SRS is new and substantially differs from the conduit affiliate concept, such conduit affiliate representations do not capture all counterparties that may be SRSs and may capture entities that fall within the conduit affiliate concept but are excluded from the definition of SRS.

E. Foreign Branch and Swap Conducted Through a Foreign Branch

1. Proposed Rule

The Commission proposed that the term ''foreign branch'' would mean an office of a U.S. person that is a bank that: (1) Is located outside the United States; (2) operates for valid business reasons; (3) maintains accounts independently of the home office and of the accounts of other foreign branches, with the profit or loss accrued at each branch determined as a separate item for each foreign branch; and (4) is engaged in the business of banking or finance and is subject to substantive regulation in banking or financing in the jurisdiction where it is located.[218]

The Commission also proposed that the term ''swap conducted through a foreign branch'' would mean a swap entered into by a foreign branch where: (1) The foreign branch or another foreign branch is the office through which the U.S. person makes and receives payments and deliveries under the swap pursuant to a master netting or similar trading agreement, and the documentation of the swap specifies that the office for the U.S. person is such foreign branch; (2) the swap is entered into by such foreign branch in its normal course of business; and (3) the swap is reflected in the local accounts of the foreign branch.[219] In the Proposed Rule, the Commission stated that the second prong of the definition (whether the swap is entered into by such foreign branch in the normal course of business) is intended as an anti-evasion measure to prevent a U.S. bank from simply routing swaps for booking in a foreign branch so that the swap would be treated as a swap conducted through a foreign branch for purposes of the SD and MSP registration thresholds or for purposes of certain regulatory requirements applicable to registered SDs or MSPs. To satisfy this prong, the Commission proposed that it must be the normal course of business for employees located in the branch (or another foreign branch of the U.S. bank) to enter into the type of swap in question. The Commission stated that this requirement would not prevent personnel of the U.S. bank located in the U.S. from participating in the negotiation or execution of the swap so long as the swaps that are booked in the foreign branch are primarily entered into by personnel located in the branch (or another foreign branch of the U.S. bank).[220]

2. Summary of Comments

While IIB/SIFMA and JFMC/IBAJ supported the proposed definition of ''foreign branch,'' noting that it was consistent with the definition given to the term in the Guidance, Better Markets recommended that the definition include a requirement that the foreign branch be operated pursuant to U.S. banking laws and regulations and in compliance with applicable restrictions. Better Markets stated that the addition of this prong adds no additional burden and ensures a foreign branch cannot be established outside of the considered restrictions and substantive requirements of U.S. law.

With respect to the proposed definition of a ''swap conducted through a foreign branch,'' Better Markets recommended that the Commission require that the swap be arranged, negotiated, and executed on behalf of the foreign branch solely by persons located outside the United States, rather than permit personnel of the U.S. bank located in the U.S. to participate in the negotiation or execution of a swap so long as the swaps that are booked in the foreign branch are primarily entered into by personnel located in the branch (or another foreign branch of the U.S. bank). Better Markets believes that this formulation defers too significantly to the foreign branches themselves to decide whether the ''primarily'' restriction has been met, and, instead recommends that the Commission adopt a foreign branch booking restriction that harmonizes with the SEC's approach. Better Markets argues that such restriction is necessary because foreign branches remain part of the U.S. person in the most critical, risk-related respects.

IIB/SIFMA and JFMC/IBAJ, on the other hand, supported the proposed definition, noting that a requirement that the personnel agreeing to a swap be located in the foreign branch is not necessary because the location of a U.S. bank's employees in connection with a particular swap does not determine whether that swap presents risks to the United States. IIB/SIFMA further argued that because foreign branches of a U.S. bank are generally subject to foreign rules when transacting with non-U.S. counterparties regardless of whether the bank's U.S. personnel are involved, applying additional U.S. rules to swaps with non-U.S. counterparties based on the involvement of U.S. personnel causes market distortions by discouraging non-U.S. counterparties from interacting with U.S. personnel. IIB/SIFMA stated further that since 2013 many U.S. banks have had to rearrange their front office coverage of non-U.S. counterparties in order to address this concern and adoption of the proposed definition would help to reverse this damaging trend.

3. Final Rule and Commission Response

Having considered the foregoing comments, the Commission has determined to adopt the definitions of ''foreign branch'' and ''swap conducted through a foreign branch'' as proposed.[221] Regarding Better Markets' recommendation that a fifth prong be added to the definition of ''foreign branch'' to more closely align the definition with the definitions used by the prudential regulators, as noted below, the definition of ''foreign branch'' proposed by the Commission is consistent with the definitions of ''foreign branch'' in the regulations of the Federal Reserve Board, the Office of the Comptroller of the Currency

[218] Proposed § 23.23(a)(2). *See* Proposed Rule, 85 FR at 966–968.

[219] Proposed § 23.23(a)(16). *See* Proposed Rule, 85 FR at 966–968.

[220] *See* Proposed Rule, 85 FR at 968.

[221] Final § 23.23(a)(2) and (16).

(''OCC''), and the Federal Deposit Insurance Corporation (''FDIC'').[222]

Regarding Better Markets' comment that a foreign branch should be treated as a U.S. person unless the employees negotiating and agreeing to the terms of the swap are exclusively located in a foreign branch, the Commission responds that such a prescriptive limitation is not required to prevent evasion of the Commission's swap requirements through booking strategies. By requiring swaps to be entered into by a foreign branch in its normal course of business, primarily by personnel located in the foreign branch, the definition proposed by the Commission provides a workable standard of review that will permit the Commission to detect evasive booking strategies while not discouraging non-U.S. counterparties from interacting with U.S. personnel.

The Commission is adopting the factors listed in the proposed definition of ''foreign branch'' for determining when an entity is considered a foreign branch for purposes of the Final Rule.[223] The requirement that the foreign branch be located outside of the United States is consistent with the stated goal of identifying certain swap activity that is not conducted within the United States. The requirements that the foreign branch maintain accounts independent of the U.S. entity,[224] operate for valid business reasons, and be engaged in the business of banking or finance and be subject to substantive banking or financing regulation in its non-U.S. jurisdiction will prevent an entity from setting up shell operations outside the United States in a jurisdiction without substantive banking or financial regulation in order to evade Dodd-Frank Act requirements and CFTC regulations.[225] This definition incorporates concepts from the Federal Reserve Board's Regulation K,[226] the FDIC's international banking regulation,[227] and the OCC's ''foreign branch'' definition.[228]

The definition of ''foreign branch'' in the Final Rule is also consistent with the SEC's approach, which, for purposes of security-based swap dealer regulation, defines a foreign branch as any branch of a U.S. bank that: (1) Is located outside the United States; (2) operates for valid business reasons; and (3) is engaged in the business of banking and is subject to substantive banking regulation in the jurisdiction where located.[229] The Commission's intention is to ensure that the definition provides sufficient clarity as to what constitutes a ''foreign branch''—specifically, an office outside of the U.S. that has independent accounts from the home office and other branches—while striving for greater regulatory harmony with the SEC.

A foreign branch does not include an affiliate of a U.S. bank that is incorporated or organized as a separate legal entity.[230] For similar reasons, the Commission declines in the Final Rule to recognize foreign branches of U.S. persons separately from their U.S. principal for purposes of registration.[231] That is, if the foreign branch engages in swap activity in excess of the relevant SD or MSP registration thresholds, as discussed further below, the U.S. person would be required to register, and the registration would encompass the foreign branch. However, upon consideration of principles of international comity and the factors set forth in the Restatement, rather than broadly excluding foreign branches from the ''U.S. person'' definition, the Commission is calibrating the requirements for counting certain swaps entered into through a foreign branch, as described in sections III.B.2 and IV.B.2, and calibrating the requirements otherwise applicable to foreign branches of a registered U.S. SD, as discussed in section VI. One of the benefits, as discussed below, will be to enable foreign branches of U.S. banks to have greater access to foreign markets.

The definition of ''swap conducted through a foreign branch'' identifies the type of swap activity for which the foreign branch performs key dealing functions outside the United States. Because a foreign branch of a U.S. bank is not a separate legal entity, the first prong of the definition clarifies that the foreign branch must be the office of the U.S. bank through which payments and deliveries under the swap are made. This approach is consistent with the standard ISDA Master Agreement, which requires that each party specify an ''office'' for each swap, which is generally where a party ''books'' a swap and/or the office through which the party makes and receives payments and deliveries.[232]

The second prong of the definition (whether the swap is entered into by such foreign branch in the normal course of business) is intended as an anti-evasion measure to prevent a U.S. bank from simply routing swaps for booking in a foreign branch so that the swap would be treated as a swap conducted through a foreign branch for purposes of the SD and MSP registration thresholds or for purposes of certain regulatory requirements applicable to registered SDs or MSPs. To satisfy this prong, it must be the normal course of business for employees located in the branch (or another foreign branch of the U.S. bank) to enter into the type of swap in question. This requirement should not prevent personnel of the U.S. bank located in the U.S. from participating in the negotiation or execution of the swap so long as the swaps that are booked in the foreign branch are primarily entered into by personnel located in the branch (or another foreign branch of the U.S. bank). As noted above, the Commission

[222] *See infra* notes 226- 228, and accompanying text.

[223] As discussed in sections III.B.2 and IV.B.2, *infra,* the Final Rule does not require an Other Non-U.S. Person to count toward its SD and MSP threshold calculations swaps conducted through a foreign branch of a registered U.S. SD.

[224] The Commission notes that national banks operating foreign branches are required under section 25 of the Federal Reserve Act (''FRA'') to conduct the accounts of each foreign branch independently of the accounts of other foreign branches established by it and of its home office, and are required at the end of each fiscal period to transfer to their general ledgers the profit or loss accrued at each branch as a separate item. 12 U.S.C. 604. The FRA is codified at 12 U.S.C. 221 *et seq.*

[225] As discussed below, the Commission is concerned that the material terms of a swap would be negotiated or agreed to by employees of the U.S. bank that are located in the United States and then be routed to a foreign branch so that the swap would be treated as a swap with the foreign branch for purposes of the SD and MSP registration thresholds or for purposes of certain regulatory requirements applicable to registered SDs or MSPs.

[226] Regulation K is a regulation issued by the Federal Reserve Board under the authority of the FRA; the Bank Holding Company Act of 1956 (''BHC Act'') (12 U.S.C. 1841 *et seq.*); and the International Banking Act of 1978 (''IBA'') (12 U.S.C. 3101 *et seq.*). Regulation K sets forth rules governing the international and foreign activities of U.S. banking organizations, including procedures for establishing foreign branches to engage in international banking. 12 CFR part 211. Under Regulation K, a ''foreign branch'' is defined as ''an office of an organization (other than a representative office) that is located outside the country in which the organization is legally established and at which a banking or financing business is conducted.'' 12 CFR 211.2(k).

[227] 12 CFR part 347 is a regulation issued by the FDIC under the authority of the Federal Deposit Insurance Act (12 U.S.C. 1828(d)(2)), which sets forth rules governing the operation of foreign branches of insured state nonmember banks. Under 12 CFR 347.102(j), a ''foreign branch'' is defined as an office or place of business located outside the United States, its territories, Puerto Rico, Guam, American Samoa, the Trust Territory of the Pacific Islands, or the Virgin Islands, at which banking operations are conducted, but does not include a representative office.

[228] 12 CFR 28.2 (defining ''foreign branch'' as an office of a national bank (other than a representative office) that is located outside the United States at which banking or financing business is conducted).

[229] *See* 17 CFR 240.3a71–3(a)(2).

[230] This is similar to the approach described in the Guidance. *See* Guidance, 78 FR at 45328–45329.

[231] This is similar to the approach described in the Guidance. *See id.* at 45315, 45328–45329.

[232] The ISDA Master Agreement defines ''office'' as a branch or office of a party, which may be such party's head or home office. *See* 2002 ISDA Master Agreement, available at *https://www.isda.org/book/2002-isda-master-agreement-english/library.*

believes this is a workable standard of review that will permit the Commission to detect evasive booking strategies by examining the types of swaps booked in the foreign branch and determining whether any type of swap is primarily entered into by personnel located in the United States.

With respect to the third prong, where a swap is with the foreign branch of a U.S. bank, it generally would be reflected in the foreign branch's accounts.

F. Swap Entity, U.S. Swap Entity, and Non-U.S. Swap Entity

The Commission proposed that the term ''swap entity'' would mean a person that is registered with the Commission as a SD or MSP pursuant to the CEA.[233] In addition, the Commission proposed to define ''U.S. swap entity'' as a swap entity that is a U.S. person, and ''non-U.S. swap entity'' as a swap entity that is not a U.S swap entity.[234]

The Commission did not receive any comments on these proposed definitions, and is adopting them as proposed.[235]

G. U.S. Branch

The Commission proposed that the term ''U.S. branch'' would mean a branch or agency of a non-U.S. banking organization where such branch or agency: (1) Is located in the United States; (2) maintains accounts independently of the home office and other U.S. branches, with the profit or loss accrued at each branch determined as a separate item for each U.S. branch; and (3) engages in the business of banking and is subject to substantive banking regulation in the state or district where located.[236]

The only comment the Commission received on this definition was from JFMC/IBAJ, stating that they generally supported the proposed new definition, as they believe it provides a clear and objective standard and provides market participants with legal certainty. Thus, the Commission is adopting the definition of ''U.S. branch'' as proposed.[237]

H. Swap Conducted Through a U.S. Branch

1. Proposed Rule

The Commission proposed that the term ''swap conducted through a U.S. branch'' would mean a swap entered into by a U.S. branch where: (1) The U.S. branch is the office through which the non-U.S. person makes and receives payments and deliveries under the swap pursuant to a master netting or similar trading agreement, and the documentation of the swap specifies that the office for the non-U.S. person is such U.S. branch; or (2) the swap is reflected in the local accounts of the U.S. branch.[238]

2. Summary of Comments

The same as for the definition of ''U.S. branch'' above, JFMC/IBAJ generally supported the proposed definition of ''swap conducted through a U.S. branch,'' as they believe it provides a clear and objective standard and provides market participants with legal certainty. However, JFMC/IBAJ, CS, and IIB/SIFMA asked the Commission to conform the definition to the definition of ''swap conducted through a foreign branch'' by (1) including a ''normal course of business'' prong, and (2) applying the definition conjunctively rather than disjunctively. JFMC/IBAJ stated that they see no policy rationale or countervailing policy benefit of these inconsistencies. CS agreed, stating that, as a matter of policy, it encourages the CFTC to provide consistent flexibility for U.S. branches and foreign branches. IIB/SIFMA stated that, in accordance with principles of international comity, the Commission should instead take a balanced and symmetric approach to recognizing when home versus host country regulators have an interest in applying their rules and that the Proposed Rule offers no justification for this asymmetric approach. ISDA also requested that the Commission apply the definition conjunctively, stating that only when a swap is booked at a particular entity can it be considered a swap transaction that is attributed to such an entity.

3. Final Rule—Swap Booked in a U.S. Branch

After carefully considering the comments, the Commission is adopting the definition with certain modifications reflected in the rule text in this release.[239] The Commission is removing the first prong of the definition such that the only relevant factor is whether the swap is reflected in the local accounts of the U.S. branch, meaning swaps for which the U.S. branch holds the risks and rewards, with the swap being accounted for as an obligation of the branch on the balance sheet of the U.S. branch under applicable accounting standards[240] and under regulatory reporting requirements[241] (*i.e.,* the swap is ''booked'' in the U.S. branch). This standard captures activity of non-U.S. banking organizations taking place in their U.S. branches that should be treated as taking place in the United States to prevent evasion of CFTC rules by such organizations. As discussed in the Proposed Rule, in the case of the swap activities of the U.S. branches of non-U.S. banking organizations, the Commission has determined that the location of personnel involved in arranging, negotiating, and execution activities will not be relevant for application of the Final Rule.[242] For this reason, the Commission had intended in the Proposed Rule only to reach swaps that are booked in the United States under the definition of ''swap conducted through a U.S. branch.''

The Commission now understands that a U.S. branch may be listed as the office through which a non-U.S. person makes and receives deliveries under a swap or as the office identified in the master, netting, or similar trading agreement without the swap being booked in a U.S. branch. Commenters explained, for example, that the U.S. branch is often listed for payments and deliveries for swaps denominated in U.S. Dollars even where the risk/benefit of the swap resides outside the United States.

Further, to emphasize that booking is the focus of the definition, the Commission is changing the term from ''swap conducted through a U.S. branch'' to ''swap booked in a U.S. branch'' (and, accordingly, revising the definitions of ''foreign-based swap'' and ''foreign counterparty'' below to reflect this change in terminology).

In response to comments objecting to the differences in the proposed definitions of ''swap conducted through a foreign branch'' and ''swap conducted through a U.S. branch,'' the Commission

[233] *See* Proposed § 23.23(a)(15); Proposed Rule, 85 FR at 968, 1003.

[234] *See* Proposed § 23.23(a)(10) and (23); Proposed Rule, 85 FR at 968, 1003.

[235] Final § 23.23(a)(11), (18), and (24).

[236] *See* Proposed § 23.23(a)(20); Proposed Rule, 85 FR at 968, 1003.

[237] Final § 23.23(a)(21).

[238] *See* Proposed § 23.23(a)(17); Proposed Rule, 85 FR at 968, 1003.

[239] Final § 23.23(a)(16).

[240] Or would be accounted for on its balance sheet under applicable accounting standards if the U.S. branch were a separate legal entity.

[241] For example, the swap is included in the non-U.S. person's Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks published by the Federal Financial Institution Examinations Council (FFIEC 002).

[242] *See infra* section V; Proposed Rule, 85 FR at 978.

is retaining these differences because, as a general matter, U.S. swap entities should be subject to all of the Commission's Title VII requirements set forth in the Final Rule. Because classifying a swap as a ''swap conducted through a foreign branch'' makes a U.S. swap entity eligible for certain exceptions from these requirements and substituted compliance for the swap under the Final Rule, merely booking a swap in the foreign branch is not sufficient for a U.S. swap entity to qualify for these exceptions and substituted compliance. Rather, the U.S. swap entity is required also to show that the swap is a transaction of a type that is endemic to the foreign market (*i.e.,* that it is a type of transaction entered into by personnel in the foreign branch in the normal course of the business of the branch, rather than a transaction more normally entered into in a different location and merely booked in the foreign branch to evade CFTC regulatory requirements). Hence, as discussed above, the Commission is including a ''normal course of business'' prong in the definition of ''a swap conducted through a foreign branch'' and requiring that all three prongs of the definition be satisfied.

As noted in the Proposed Rule and consistent with the Commission's approach to foreign branches, a U.S. branch of a non-U.S. banking organization does not include a U.S. affiliate of the organization that is incorporated or organized as a separate legal entity. Also consistent with this approach, the Commission declines in the Final Rule to recognize U.S. branches of non-U.S. banking organization separately from their non-U.S. principal for purposes of registration.

I. Foreign-Based Swap and Foreign Counterparty

1. Proposed Rule

The Commission proposed that the term ''foreign-based swap'' would mean: (1) A swap by a non-U.S. swap entity, except for a swap conducted through a U.S. branch; or (2) a swap conducted through a foreign branch.[243] Further, the term ''foreign counterparty'' would mean: (1) A non-U.S. person, except with respect to a swap conducted through a U.S. branch of that non-U.S. person; or (2) a foreign branch where it enters into a swap in a manner that satisfies the definition of a swap conducted through a foreign branch.[244] Under the Proposed Rule, together with the proposed defined terms ''foreign branch,'' ''swap conducted through a foreign branch,'' ''U.S. branch,'' and ''swap conducted through a U.S. branch,'' these terms were to be used to determine which swaps would be foreign swaps of non-U.S. swap entities and foreign branches of U.S. swap entities, for which certain relief from Commission requirements would be available under the Proposed Rule, and which swaps would be treated as domestic swaps not eligible for such relief.

2. Summary of Comments

AIMA was supportive of the definition of ''foreign counterparty'' and, in particular, its application to CIVs. However, JFMC/IBAJ requested that the Commission expand the definition of ''foreign-based swap'' and ''foreign counterparty'' under the proposed exceptions from the group B and C requirements (described in sections VI.A.2 and VI.A.3 below) to cover swaps conducted through the U.S. branch of a non-U.S. swap entity. JFMC/IBAJ stated that these are swap trades between two non-U.S. persons and thus should be governed by the home country regulation of the non-U.S. persons according to principles of international comity, and that there is no material importation of risk to the U.S. financial system and hence a lack of sufficient jurisdictional nexus for purposes of CEA section 2(i). JBA similarly requested that, generally, swap requirements not apply to U.S. branches in a different manner than the related non-U.S person.

3. Final Rule

After carefully considering the comments, the Commission is adopting the definitions of ''foreign-based swap'' and ''foreign counterparty'' as proposed, with a minor technical modification included in the rule text in this release.[245] Specifically, to reflect that the term ''swap conducted through a U.S. branch'' is being replaced with the term ''swap booked in a U.S. branch,'' each of the definitions of ''foreign-based swap'' and ''foreign counterparty'' is being revised to replace the term ''swap conducted through a U.S. branch'' with the term ''swap booked in a U.S. branch.''

When a swap is booked in a U.S. branch of a non-U.S. swap entity, that swap is part of the U.S. swap market, and, accordingly, the group B and group C requirements (described in sections VI.A.2 and VI.A.3 below) should generally apply.[246] Therefore, the Commission has determined to carve out a swap booked in a U.S. branch from the definitions of ''foreign-based swap'' and ''foreign counterparty.''

As discussed in the Proposed Rule, the Commission is using the terms ''foreign-based swap'' and ''foreign counterparty'' to identify the types of swaps that are eligible for certain relief, consistent with section 2(i) of the CEA, in order that swaps that demonstrate sufficient indicia of being domestic generally remain subject to the Commission's requirements under the Final Rule, notwithstanding that the swap is entered into by a non-U.S. swap entity or a foreign branch of a U.S. swap entity. Otherwise, an entity or branch might simply be established outside of the United States to evade Dodd-Frank Act requirements and CFTC regulations.

As the Commission has previously stated, it has a strong supervisory interest in regulating swap activities that occur in the United States.[247] However, consistent with section 2(i) of the CEA, foreign swaps of non-U.S. swap entities and foreign branches of U.S. swap entities should be eligible for relief from certain of the Commission's requirements. Accordingly, certain exceptions from the group B and group C requirements and portions of the Commission's substituted compliance regime (discussed below in sections VI.B and VI.C), are designed to apply only to certain foreign swaps of non-U.S. swap entities and foreign branches of U.S. swap entities that the Commission believes should be treated as occurring outside the United States. Specifically, these provisions are applicable only to a swap by a non-U.S. swap entity—except for a swap booked in a U.S. branch—and a swap conducted through a foreign branch such that it satisfies the definition of a ''foreign-based swap'' above. They are generally not applicable to swaps of non-U.S. swap entities that are booked in a U.S. branch of that swap entity, and swaps of foreign branches of U.S. swap entities where the foreign branch does not enter into the swaps in a manner that satisfies the definition of a swap conducted through a foreign branch, because the

[243] *See* Proposed § 23.23(a)(4); Proposed Rule, 85 FR at 968–969, 1002.

[244] *Id.*

[245] Final § 23.23(a)(4) and (5).

[246] The Commission notes that swap activities of the U.S. branches of non-U.S. banking organizations take place inside the United States and, thus, section 2(i)'s applicability (*i.e.,* to activities ''outside the U.S.'') is not implicated. Nevertheless, as discussed in sections VI.B and VI.C, *infra,* the Commission has determined under the Final Rule to provide certain exceptions from application of the group C requirements and the availability of substituted compliance for the group B requirements for certain swaps booked in the U.S. branches of non-U.S. swap entities.

[247] *See* Guidance, 78 FR at 45350, n.513.

entrance into a swap by a U.S. swap entity (through its foreign branch) or a U.S. branch of a non-U.S. swap entity under these circumstances, demonstrates sufficient indicia of being a domestic swap to be treated as such for purposes of the Final Rule. Similarly, in certain cases, the availability of an exception or substituted compliance for a swap depends on whether the counterparty to such a swap qualifies as a ''foreign counterparty'' under the Final Rule. The Commission is establishing this requirement to ensure that foreign-based swaps of swap entities in which their counterparties demonstrate sufficient indicia of being domestic and, thus, trigger the Commission's supervisory interest in domestic swaps, remain subject to the Commission requirements under the Final Rule.

The Commission's approach in the Final Rule to limit certain relief for U.S. branches of non-U.S. swap entities is parallel to the Commission's approach in the Final Rule to provide certain exceptions from Commission requirements or substituted compliance for certain transactions of foreign branches of U.S. swap entities to take into account the supervisory interest of local regulators, as discussed below in section VI.

III. Cross-Border Application of the Swap Dealer Registration Threshold

CEA section 1a(49) defines the term ''swap dealer'' to include any person that: (1) Holds itself out as a dealer in swaps; (2) makes a market in swaps; (3) regularly enters into swaps with counterparties as an ordinary course of business for its own account; or (4) engages in any activity causing the person to be commonly known in the trade as a dealer or market maker in swaps (collectively referred to as ''swap dealing,'' ''swap dealing activity,'' or ''dealing activity'').[248] The statute also requires the Commission to promulgate regulations to establish factors with respect to the making of a determination to exempt from designation as an SD an entity engaged in a de minimis quantity of swap dealing.[249]

In accordance with CEA section 1a(49), the Commission issued the Entities Rule,[250] which, among other things, further defined the term ''swap dealer'' and excluded from designation as an SD any entity that engages in a de minimis quantity of swap dealing with or on behalf of its customers.[251] Specifically, the definition of ''swap dealer'' in § 1.3 provides that a person shall not be deemed to be an SD as a result of its swap dealing activity involving counterparties unless, during the preceding 12 months, the aggregate gross notional amount of the swaps connected with those dealing activities exceeds the de minimis threshold.[252] Paragraph (4) of that definition further requires that, in determining whether its swap dealing activity exceeds the de minimis threshold, a person must include the aggregate gross notional amount of the swaps connected with the dealing activities of its affiliates under common control.[253] For purposes of the Commission's interpretation of the aggregation requirement in the cross-border context as set forth in this release, the Commission construes ''affiliates under common control'' by reference to the Entities Rule, which defined control as the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise.[254] Accordingly, any reference in the Commission's aggregation interpretation to ''affiliates under common control'' with a person includes affiliates that are controlling, controlled by, or under common control with such person.

The Commission is now adopting rules to address how the de minimis threshold should apply to the cross-border swap dealing transactions of U.S. and non-U.S. persons. Specifically, the Final Rule identifies when a potential SD's cross-border dealing activities should be included in its de minimis threshold calculation and when they may properly be excluded. As discussed below, whether a potential SD includes a particular swap in its de minimis threshold calculation depends on how the entity and its counterparty are classified (*e.g.,* U.S. person, SRS, etc.) and, in some cases, the jurisdiction in which a non-U.S. person is regulated.

A. U.S. Persons

The Commission is adopting, as proposed and consistent with the Guidance, the requirement that a U.S. person include all of its swap dealing transactions in its de minimis threshold calculation without exception.[255] The Commission did not receive comments regarding this requirement. As discussed in section II.B above, the term ''U.S. person'' encompasses a person that, by virtue of being domiciled, organized, or having its principal place of business in the United States, raises the concerns intended to be addressed by the Dodd-Frank Act, regardless of the U.S. person status of its counterparty. In addition, a person's status as a U.S. person is determined at the entity level and, thus, a U.S. person includes the swap dealing activity of operations that are part of the same legal person, including those of its foreign branches. Therefore, a U.S. person includes in its SD de minimis threshold calculation dealing swaps entered into by a foreign branch of the U.S. person.[256]

B. Non-U.S. Persons

Under the Final Rule, as discussed in more detail below, whether a non-U.S. person needs to include a swap in its de minimis threshold calculation depends on the non-U.S. person's status, the status of its counterparty, and, in some cases, the jurisdiction in which the non-U.S. person is regulated. Specifically, the Final Rule requires a person that is a Guaranteed Entity or an SRS to count all of its dealing swaps towards the de minimis threshold.[257] In addition, an Other Non-U.S. Person is required to count dealing swaps with a U.S. person toward its de minimis threshold calculation, except for swaps conducted through a foreign branch of a registered U.S. SD.[258] Further, subject to certain exceptions, the Final Rule requires an

[248] 7 U.S.C. 1a(49)(A). In general, a person that satisfies any one of these prongs is deemed to be engaged in swap dealing activity.

[249] 7 U.S.C. 1a(49)(D).

[250] Entities Rule, 77 FR 30596.

[251] 17 CFR 1.3, Swap dealer, paragraph (4); Entities Rule, 77 FR 30596.

[252] 17 CFR 1.3, Swap dealer, paragraph (4)(i)(A). The de minimis threshold is set at $8 billion, except with regard to swaps with special entities for which the threshold is $25 million. *See id.,* paragraphs (4)(i)(A)–(B). *See generally* De Minimis Exception to the Swap Dealer Definition, 83 FR 56666 (Nov. 13, 2018).

[253] 17 CFR 1.3, Swap dealer, paragraph (4)(i)(A).

[254] *See* Entities Rule, 77 FR at 30631 n.437.

[255] Final § 23.23(b)(1). *See* Proposed Rule, 85 FR at 970–971, 1004; Guidance, 78 FR at 45326.

[256] Proposed Rule, 85 FR at 970–971. This approach mirrors the SEC's approach in its cross-border rule. *See* 17 CFR 240.3a71–3(b)(1)(i); SEC Cross-Border Rule, 79 FR at 47302, 47371.

[257] As discussed in section II.C, *supra,* for purposes of this release and ease of reading, a non-U.S. person whose obligations under a swap are subject to a guarantee by a U.S. person is being referred to as a ''Guaranteed Entity.'' A non-U.S. person may be a Guaranteed Entity with respect to certain swaps and not others (including, *e.g.,* where the non-U.S. person is guaranteed only with respect to its swaps with certain counterparties). Thus, a non-U.S. person could be a Guaranteed Entity or an Other Non-U.S. Person, depending on the specific swap.

[258] As stated, ''swap conducted through a foreign branch'' means a swap entered into by a foreign branch where: (1) The foreign branch or another foreign branch is the office through which the U.S. person makes and receives payments and deliveries under the swap pursuant to a master netting or similar trading agreement, and the documentation of the swap specifies that the office for the U.S. person is such foreign branch; (2) the swap is entered into by such foreign branch in its normal course of business; and (3) the swap is reflected in the local accounts of the foreign branch.

Other Non-U.S. Person to count dealing swaps toward its de minimis threshold calculation if the counterparty to such swaps is a Guaranteed Entity.

1. Swaps by a Significant Risk Subsidiary

The Commission proposed to require an SRS to include all of its dealing swaps in its de minimis threshold calculation without exception.[259]

IIB/SIFMA stated that, generally, the Commission should not require a non-U.S. person, whether or not it is an SRS or other FCS, to include dealing swaps with a non-U.S. person in its SD de minimis threshold calculation when the risk of such swaps is transferred to an affiliated, registered U.S. SD. In such a situation, IIB/SIFMA asserted that there is no significant potential for risk to the United States or evasion of the Dodd-Frank Act because the Commission already can exercise appropriate regulatory oversight through direct regulation of the registered SD, which is subject to Dodd-Frank Act provisions such as risk management requirements and Commission or prudential regulator margin and capital requirements. IIB/SIFMA argued that this consideration underlies the Commission's decision to exclude affiliates of a registered SD from the ''conduit affiliate'' definition in the Guidance, as well as the similar approach taken by the SEC in its implementation of the Dodd-Frank Act.

After considering this comment, the Commission is adopting this requirement as proposed.[260] As discussed in section II.D above, the SRS test identifies a person that, by virtue of being a significant subsidiary of a U.S. person, and not being subject to prudential supervision as a subsidiary of a BHC or IHC, or subject to comparable capital and margin rules, raises the concerns intended to be addressed by the Dodd-Frank Act requirements addressed by the Final Rule, regardless of the status of its counterparty as a U.S. person or non-U.S. person. The Commission believes that treating an SRS differently from a U.S. person could create a substantial regulatory loophole, incentivizing U.S. persons to conduct their dealing business with non-U.S. persons through SRSs to avoid application of the Dodd-Frank Act SD requirements. Allowing swaps entered into by SRSs, which have the potential to affect the ultimate U.S. parent entity and U.S. commerce, to be treated differently depending on how the parties structure their transactions could undermine the effectiveness of the Dodd-Frank Act swaps provisions and related Commission regulations addressed by the Final Rule. Applying the same standard to similar transactions helps to limit those incentives and regulatory implications. Because the SRS definition is a risk-based test, the Commission has determined not to include a carve-out for back-to-back swaps to SDs, as was provided in the Guidance for conduit affiliates. Additionally, the SRS definition, as adopted in the Final Rule, already includes a carve-out for affiliates of BHCs and IHCs. This approach allows for streamlined application of the rule, and the comment letters have not identified specific downsides to this approach.[261]

In addition, a person's status as an SRS is determined at the entity level and, thus, an SRS is required to include in its SD de minimis threshold calculation the dealing swaps of its operations that are part of the same legal person, including those of its branches.[262]

The Proposed Rule also provided that an Other Non-U.S. Person would not be required to count a dealing swap with an SRS toward its de minimis threshold calculation, unless the SRS was also a Guaranteed Entity (and no exception applied).[263] JFMC/IBAJ supported this approach, while JBA asserted that an Other Non-U.S. Person should not have to count a swap entered into with a non-U.S. person in any circumstance. As noted above, an SRS is required to count all of its dealing swaps. However, the Commission continues to believe that where an Other Non-U.S. Person is entering into a dealing swap with an SRS, requiring the Other Non-U.S. Person to count the swap towards its de minimis threshold could cause the Other Non-U.S. Person to stop engaging in swap activities with SRSs. Though an SRS is required to count all of its dealing swaps, for the reasons stated above, the Commission believes that it is important to ensure that SRSs, particularly ones that are a commercial or non-financial entity that do not engage in swap dealing activities, continue to have access to swap liquidity from Other Non-U.S. Persons for hedging or other non-dealing purposes.

2. Swaps With a U.S. Person

Consistent with the Guidance, the Commission proposed to require a non-U.S. person to count all dealing swaps with a counterparty that is a U.S. person toward its de minimis threshold calculation, except for swaps with a counterparty that is a foreign branch of a registered U.S. SD if such swaps meet the definition of being ''conducted through a foreign branch'' of such registered SD.[264]

IIB/SIFMA, JFMC/IBAJ, and JBA supported allowing an Other Non-U.S. Person to exclude swap dealing transactions conducted through a foreign branch of a registered SD counterparty. IIB/SIFMA agreed that the Commission's regulatory interest in these swaps is not sufficient to warrant a competitive disadvantage for foreign branches of U.S. SDs, especially considering that other Dodd-Frank Act requirements, such as margin, mitigate the risk of these swaps to the U.S. SD. Additionally, IIB/SIFMA stated that the exclusion helps prevent market fragmentation by enabling Other Non-U.S. Persons to access liquidity provided by U.S. SDs through their foreign branches. On the other hand, AFR asserted that the Proposed Rule would allow branches of U.S. persons, which are actually formally and legally part of the parent U.S. organization, to effectively act as non-U.S. persons.

After considering the comments, the Commission is adopting this aspect of the cross-border application of the SD registration threshold as proposed.[265] As discussed in section II.B, the term ''U.S. person'' encompasses persons that inherently raise the concerns intended to be addressed by the Dodd-Frank Act regardless of the U.S. person status of their counterparty. In the event of a default or insolvency of a non-U.S. SD, the SD's U.S. counterparties could be adversely affected. A credit event, including funding and liquidity problems, downgrades, default, or insolvency at a non-U.S. SD could therefore have a direct and significant adverse effect on its U.S. counterparties, which could in turn create the risk of disruptions to the U.S. financial system.[266]

Allowing a non-U.S. person to exclude swaps conducted through a foreign branch of a registered SD counterparty from its de minimis threshold calculation is consistent with the Guidance.[267] In response to AFR's comment that the Proposed Rule allows foreign branches of U.S. persons to effectively act as non-U.S. persons, the

[259] Proposed § 23.23(b)(1); Proposed Rule, 85 FR at 971, 1004.

[260] Final § 23.23(b)(1).

[261] *See* Proposed Rule, 85 FR at 971.

[262] *Id.*

[263] *Id.*

[264] Proposed § 23.23(b)(2)(i); Proposed Rule, 85 FR at 971–972, 1004. *See* Guidance, 78 FR at 45323–45324.

[265] Final § 23.23(b)(2)(i).

[266] Proposed Rule, 85 FR at 971–972.

[267] *Id. See* Guidance, 78 FR at 45323–45324.

Commission continues to believe that its regulatory interest in these swaps is not sufficient to warrant creating a potential competitive disadvantage for foreign branches of U.S. SDs with respect to their foreign entity competitors by requiring non-U.S. persons to count trades with them toward their de minimis threshold calculations. In this regard, a swap conducted through a foreign branch of a registered SD triggers certain Dodd-Frank Act transactional requirements (or comparable requirements), particularly margin requirements, and thus, such swap activity is not conducted fully outside the Dodd-Frank Act regime. Moreover, in addition to certain Dodd-Frank Act requirements that apply to such swaps, other foreign regulatory requirements may also apply similar transactional requirements to the transactions.[268] Accordingly, the Commission believes that it is appropriate and consistent with section 2(i) of the CEA to allow non-U.S. persons to exclude from their de minimis calculation any swap dealing transactions conducted through a foreign branch of a registered SD counterparty. However, this exception does not apply to Guaranteed Entities (discussed below) or SRSs (discussed above), who have to count all of their dealing swaps.

The Commission also requested comment on whether it would be appropriate to require a U.S. branch to include in its SD de minimis threshold calculation all of its swap dealing transactions, as if they were swaps entered into by a U.S. person, and whether it would be appropriate to require an Other Non-U.S. Person to include in its SD de minimis threshold calculation dealing swaps conducted through a U.S. branch of its counterparty.[269] IIB/SIFMA supported not requiring a U.S. branch of a non-U.S. banking organization to include all of its swap dealing transactions in its SD de minimis threshold calculation as if they were swaps entered into by a U.S. person or to require an Other Non-U.S. Person to include in its SD de minimis threshold calculation dealing swaps conducted through such a branch of its counterparty. IIB/SIFMA stated that swaps between a U.S. branch and an Other Non-U.S. Person do not present risks to the United States that would justify applying the Commission's SD requirements. JBA also stated that Other Non-U.S. Persons should not have to count swaps conducted through a U.S. branch of a counterparty since such an approach may lead to Other Non-U.S. Persons decreasing activity with U.S. branches.

Having considered the foregoing comments, in this Final Rule, the Commission is not requiring a U.S. branch of an Other Non-U.S. Person to count all of its swap dealing transactions in its SD threshold calculation, as if they were swaps entered into by a U.S. person. Rather, a U.S. branch is required to count swaps pursuant to the requirements for Other Non-U.S. Persons (*e.g.,* count swaps with U.S. persons, Guaranteed Entities subject to certain exceptions, etc.). Additionally, an Other Non-U.S. Person is not required to include in its SD de minimis threshold calculation dealing swaps booked in a U.S. branch of a counterparty, unless that swap has to be counted pursuant to other requirements of this Final Rule.

3. Guaranteed Swaps

(i) Swaps Entered Into by a Guaranteed Entity

In an approach that is generally consistent with the Guidance, the Commission proposed to require a non-U.S. person to include in its de minimis threshold calculation swap dealing transactions where its obligations under the swaps are guaranteed by a U.S. person.[270] No comments were received regarding this aspect of the Proposed Rule.

The Commission is adopting this requirement as proposed,[271] because the swap obligations of a Guaranteed Entity are identical, in relevant aspects, to a swap entered into directly by a U.S. person. As a result of the guarantee, the U.S. guarantor generally bears risk arising out of the swap as if it had entered into the swap directly. The U.S. guarantor's financial resources in turn enable the Guaranteed Entity to engage in dealing activity, because the Guaranteed Entity's counterparties will look to both the Guaranteed Entity and its U.S. guarantor to ensure performance of the swap. Absent the guarantee from the U.S. person, a counterparty may choose not to enter into the swap or may not do so on the same terms. In this way, the Guaranteed Entity and the U.S. guarantor effectively act together to engage in the dealing activity.[272]

Further, treating a Guaranteed Entity differently from a U.S. person could create a substantial regulatory loophole, incentivizing U.S. persons to conduct their dealing business with non-U.S. persons through non-U.S. affiliates, with a U.S. guarantee, to avoid application of the Dodd-Frank Act SD requirements. Allowing transactions that have a similar economic reality with respect to U.S. commerce to be treated differently depending on how the parties structure their transactions could undermine the effectiveness of the Dodd-Frank Act swap provisions and related Commission regulations addressed by the Final Rule. Applying the same standard to similar transactions helps to limit those incentives and regulatory implications.[273]

(ii) Swaps Entered Into With a Guaranteed Entity

The Commission also proposed to require a non-U.S. person to count dealing swaps with a Guaranteed Entity in its SD de minimis threshold calculation, except when: (1) The Guaranteed Entity is registered as an SD; or (2) the Guaranteed Entity's swaps are subject to a guarantee by a U.S. person that is a non-financial entity.[274] The Commission also invited comment on whether it should the follow the SEC's approach, which does not require a non-U.S. person that is not guaranteed by a U.S. person to count dealing swaps with a Guaranteed Entity.[275]

IIB/SIFMA, ISDA, JFMC/IBAJ, and JBA recommended that the Commission further conform this provision with the Guidance by expanding the exceptions to also cover a Guaranteed Entity that engages in de minimis swap dealing activity and is affiliated with a

[268] As noted in section I.C, *supra,* significant and substantial progress has been made in the world's primary swaps trading jurisdictions to implement the G20 swaps reform commitments.

[269] Proposed Rule, 85 FR at 973. *See* discussion of the modification of the definition of a ''swap conducted through a U.S. branch'' to be a ''swap booked in a U.S. branch'' in section II.H.3, *supra.*

[270] Proposed § 23.23(b)(2)(ii); Proposed Rule, 85 FR at 972, 1004. The Guidance stated that where a non-U.S. affiliate of a U.S. person has its swap dealing obligations with non-U.S. persons guaranteed by a U.S. person, the guaranteed affiliate generally would be required to count those swap dealing transactions with non-U.S. persons (in addition to its swap dealing transactions with U.S. persons) for purposes of determining whether the affiliate exceeds a de minimis amount of swap dealing activity and must register as an SD. Guidance, 78 FR at 45312–45313. As discussed above, the Final Rule does not require that the guarantor be an affiliate of the guaranteed person for that person to be a Guaranteed Entity.

[271] Final § 23.23(b)(2)(ii).

[272] Proposed Rule, 85 FR at 972. This view is consistent with the SEC's approach in its cross-border rule. *See* SEC Cross-Border Rule, 79 FR at 47289.

[273] Proposed Rule, 85 FR at 972.

[274] Proposed § 23.23(b)(2)(iii); Proposed Rule, 85 FR at 973, 1004.

[275] Proposed Rule, 85 FR at 974. The SEC noted that ''concerns regarding the risk posed to the United States by such security-based swaps, and regarding the potential use of such guaranteed affiliates to evade the Dodd-Frank Act . . . are addressed by the requirement that guaranteed affiliates count their own dealing activity against the de minimis thresholds when the counterparty has recourse to a U.S. person.'' SEC Cross-Border Rule, 79 FR at 47322.

registered SD. IIB/SIFMA and ISDA noted that the Commission's regulatory concerns are addressed because the Guaranteed Entity would already be required to count the swap towards its de minimis threshold. IIB/SIFMA, ISDA, and JFMC/IBAJ noted that absent this exception, Other Non-U.S. Persons may choose not to trade with Guaranteed Entities, leading to increased market fragmentation or competitive disadvantages. JFMC/IBAJ also stated that there has been no material change in the swaps market since issuance of the Guidance warranting removing this exception. JBA commented that Other Non-U.S. Persons should not have to count swaps where the non-U.S. counterparty transfers risks to an affiliated U.S. SD because of the burdens associated with such an approach, and the limited risks arising from transactions between two non-U.S. persons. JBA also recommended that the CFTC follow the SEC approach and not require a non-U.S. person to count a swap with a Guaranteed Entity because it is burdensome to assess whether a guarantee exists.

Consistent with the Guidance, the Commission is adopting, as proposed, the requirement that a non-U.S. person must count dealing swaps with a Guaranteed Entity in its SD de minimis threshold calculation, except when: (1) The Guaranteed Entity is registered as an SD; or (2) the Guaranteed Entity's swaps are subject to a guarantee by a U.S. person that is a non-financial entity.[276] Additionally, after carefully considering the comments, and to maintain consistency with the Guidance, the Commission is also adopting an exception that allows a non-U.S. person to exclude from its de minimis calculation swaps entered into with a Guaranteed Entity that is itself below the de minimis threshold and is affiliated with a registered SD.[277]

The guarantee of a swap is an integral part of the swap and, as discussed above, counterparties may not be willing to enter into a swap with a Guaranteed Entity in the absence of the guarantee. The Commission recognizes that, given the highly integrated corporate structures of global financial enterprises described above, financial groups may elect to conduct their swap dealing activity in a number of different ways, including through a U.S. person or through a non-U.S. affiliate that benefits from a guarantee from a U.S. person. Therefore, in order to avoid creating a regulatory loophole, swaps of a non-U.S. person with a Guaranteed Entity should receive the same treatment as swaps with a U.S. person. The exceptions are intended to address those situations where the risk of the swap between the non-U.S. person and the Guaranteed Entity is otherwise managed under the Dodd-Frank Act swap regime or is primarily outside the U.S. financial industry.[278] JBA supported the SEC's approach, which, as noted, does not require a non-U.S. person that is not a conduit affiliate or guaranteed by a U.S. person to count dealing swaps with any guaranteed entity toward its de minimis threshold in any case.[279] Given the broader global scope of the swaps market regulated under the Commission's swap regime versus the relatively more limited U.S.-focused scope of the security-based swap market regulated under the SEC's security-based swap regime, the Commission has determined to treat swaps with Guaranteed Entities differently.

Where an Other Non-U.S. Person enters into swap dealing transactions with a Guaranteed Entity that is a registered SD, the Commission will permit the non-U.S. person not to count its dealing transactions with the Guaranteed Entity against the non-U.S. person's de minimis threshold for two principal reasons. First, requiring the non-U.S. person to count such swaps may incentivize them to not engage in dealing activity with Guaranteed Entities, thereby contributing to market fragmentation and competitive disadvantages for entities wishing to access foreign markets. Second, one counterparty to the swap is a registered SD, and therefore is subject to comprehensive swap regulation under the oversight of the Commission.[280]

In addition, an Other Non-U.S. Person need not include in its de minimis threshold calculation its swap dealing transactions with a Guaranteed Entity where the Guaranteed Entity is guaranteed by a non-financial entity. In these circumstances, systemic risk to U.S. financial markets is mitigated because the U.S. guarantor is a non-financial entity whose primary business activities are not related to financial products and such activities primarily occur outside the U.S. financial sector.[281] For purposes of the Final Rule, the Commission interprets ''non-financial entity'' to mean a counterparty that is not an SD, an MSP, or a financial end-user (as defined in the SD and MSP margin rule in § 23.151).[282]

Lastly, as discussed, the Commission requested comment on whether it should expand the exception to not require a non-U.S. person that is not a Guaranteed Entity to count dealing swaps with a Guaranteed Entity, consistent with the SEC. IIB/SIFMA, ISDA, JFMC/IBAJ, and JBA requested a narrower version of this exception, noting that the Guidance allowed a non-U.S. person to exclude from its de minimis calculation swaps entered into with a Guaranteed Entity that is itself below the de minimis threshold and is affiliated with a registered SD. The Guidance reflected the Commission's view that when the aggregate level of swap dealing by a non-U.S. person that is not a guaranteed affiliate, considering both swaps with U.S. persons and swaps with unregistered guaranteed affiliates, exceeds the de minimis level of swap dealing, the non-U.S. person's swap dealing transactions have the requisite direct and significant connection with activities in, or effect on, commerce of the United States.[283] The Commission believes, however, that where the counterparty to a swap is a Guaranteed Entity and is not a registered SD, the Commission's regulatory concerns, such as systemic risk to U.S. financial markets, are addressed because the Guaranteed Entity engages in a level of swap dealing below the de minimis threshold and is part of an affiliated group with an SD.[284] Risk to the Guaranteed Entity should be mitigated by the SD's risk management program, which under Commission rules must take account of risks posed by affiliates and must be integrated into risk management at the consolidated entity level.[285] Including this exception also addresses concern that its elimination would discourage Other Non-U.S. Persons from entering into swaps with Guaranteed Entities, creating competitive disadvantages.

C. Aggregation Requirement

Paragraph (4) of the SD definition in § 1.3 requires that, in determining whether its swap dealing transactions exceed the de minimis threshold, a person must include the aggregate notional amount of any swap dealing transactions entered into by its affiliates

[276] Final § 23.23(b)(2)(iii)(A) and (B). *See* Guidance, 78 FR at 45324.

[277] Final § 23.23(b)(2)(iii)(C). *See* Guidance, 78 FR at 45324.

[278] Proposed Rule, 85 FR at 972.

[279] SEC Cross-Border Rule, 79 FR at 47322.

[280] Proposed Rule, 85 FR at 972.

[281] Moreover, the SRS definition includes those non-financial U.S. parent entities that meet the risk-based thresholds set out in section II.D, *supra.*

[282] Proposed Rule, 85 FR at 972.

[283] Guidance, 78 FR at 45324.

[284] *Id.*

[285] 17 CFR 23.600(c)(1)(ii).

under common control.[286] Consistent with CEA section 2(i), the Commission interprets this aggregation requirement in a manner that applies the same aggregation principles to all affiliates in a corporate group, whether they are U.S. or non-U.S. persons.

Accordingly, consistent with the Guidance, the Commission proposed to require a potential SD, whether a U.S. or non-U.S. person, to aggregate all swaps connected with its dealing activity with those of persons controlling, controlled by, or under common control with the potential SD to the extent that these affiliated persons are themselves required to include those swaps in their own de minimis threshold calculations, unless the affiliated person is itself a registered SD.[287]

Better Markets supported the proposed aggregation requirement because it would prevent structuring to avoid or evade the de minimis threshold. As discussed above in connection with the definition of ''significant risk subsidiary,'' AFR stated that it would be simple for large international banks and other significant actors to conduct dealing through foreign subsidiaries that need not be counted toward de minimis thresholds at the subsidiary level. AFR claimed that the aggregation provision is negated by the fact that affiliates which are not SRSs would not have to count non-guaranteed swaps with other non-U.S., non-SRS persons toward their own de minimis calculations. In this way, it argued that the weakness of the other definitions in the Proposed Rule affects the calculation of the de minimis registration thresholds.

Having considered these comments, the Commission is adopting this interpretation of the cross-border application of the SD registration threshold as proposed, and consistent with the Guidance.[288] Stated in general terms, the Commission's approach allows both U.S. persons and non-U.S. persons in an affiliated group to engage in swap dealing activity up to the de minimis threshold. When the affiliated group meets the de minimis threshold in the aggregate, one or more affiliate(s) (a U.S. affiliate or a non-U.S. affiliate) have to register as an SD so that the relevant swap dealing activity of the unregistered affiliates remains below the threshold. The Commission recognizes the borderless nature of swap dealing activities, in which a dealer may conduct swap dealing business through its various affiliates in different jurisdictions, and believes that its approach addresses the concern that an affiliated group of U.S. and non-U.S. persons engaged in swap dealing transactions with a significant connection to the United States may not be required to register solely because such swap dealing activities are divided among affiliates that all individually fall below the de minimis threshold. The Commission's approach ensures that the aggregate gross notional amount of applicable swap dealing transactions of all such unregistered U.S. and non-U.S. affiliates does not exceed the de minimis level.[289]

In response to AFR's comment, pursuant to the status quo under the aggregation policy set forth in the Guidance, foreign subsidiaries of U.S. persons (that are not ''conduit affiliates'' as described in the Guidance) have not counted non-guaranteed swaps with other non-U.S. persons toward their de minimis calculations and U.S. person parent entities have therefore not aggregated such swaps with their own or their affiliates' de minimis calculations. Thus, the new SRS category expands the swaps included by the aggregation requirement rather than ''negating the aggregation provision'' as claimed by AFR.

D. Certain Exchange-Traded and Cleared Swaps

The Commission proposed, in an approach that is generally consistent with the Guidance, to allow an Other Non-U.S. Person to exclude from its de minimis threshold calculation any swap that it anonymously enters into on a designated contract market (''DCM''), a swap execution facility (''SEF'') that is registered with the Commission or exempted by the Commission from SEF registration pursuant to section 5h(g) of the CEA, or a foreign board of trade (''FBOT'') that is registered with the Commission pursuant to part 48 of its regulations,[290] if such swap is also cleared through a registered or exempt derivatives clearing organization (''DCO'').[291]

IIB/SIFMA recommended that this exception be expanded to cover swaps executed anonymously by an Other Non-U.S. Person on a non-U.S. trading venue and cleared by a non-U.S. clearing organization, regardless of whether the trading venue and clearing organization are registered or exempt from registration with the Commission. IIB/SIFMA stated that: (1) With such trades, the Other Non-U.S. Person cannot determine whether the swaps would count towards the SD de minimis threshold; (2) even if the Other Non-U.S. Person was registered as an SD, the swaps generally would not be subject to the Commission's external business conduct rules; and (3) a non-U.S. clearing organization becomes the counterparty to the Other Non-U.S. Person, and therefore the swaps do not present risk to the U.S. that would justify application of the Commission's risk mitigation rules. IIB/SIFMA stated that if the Other Non-U.S. Person's original counterparty was a U.S. person, the Commission's SEF and DCO registration requirements would independently require the trading venue and clearing organization to register with the Commission or obtain an exemption from registration and, therefore, it is not necessary for the Commission to limit this exception in a manner that would indirectly expand the SEF and DCO registration requirements to non-U.S. trading venues and clearing organizations with Other Non-U.S. Person participants.

Similarly, JFMC/IBAJ generally supported the exception, but also requested that the Commission not require the clearing organization or trading venue to be registered or exempt from registration with the CFTC because, in their view, the same policy rationale of exempting cleared swaps executed anonymously on a SEF or DCM applies to swaps executed on non-U.S. trading venues or clearing organizations operating without a CFTC registration or exemption. JFMC/IBAJ also recommended that the scope be expanded to include cleared swaps executed bilaterally outside a trading venue. JBA generally supported the proposal but also recommended that the exclusion be available for all cleared swaps, regardless of whether they are anonymously entered into on a DCM, registered or exempt SEF, or an FBOT, because risk to the U.S. would be limited after the swap is cleared. JSCC recommended that a non-U.S. person should be able to exclude swaps entered into with a U.S. person from the de minimis threshold calculation, if the swap is cleared with a registered DCO or exempt DCO because any non-U.S. person-related risk arising from the

[286] 17 CFR 1.3, Swap dealer, paragraph (4).

[287] Proposed Rule, 85 FR at 972–973; Guidance, 78 FR at 45323.

[288] Proposed Rule, 85 FR at 972–973; Guidance, 78 FR at 45323.

[289] Proposed Rule, 85 FR at 972–973.

[290] The Commission considers the exception described herein also to apply with respect to an FBOT that provides direct access to its order entry and trade matching system from within the U.S. pursuant to no-action relief issued by Commission staff.

[291] Proposed § 23.23(d); Proposed Rule, 85 FR at 973, 1004. *See* Guidance, 78 FR at 45325.

swap will be replaced and instead managed by the DCO.

Better Markets stated that the exception must be amended to limit the exclusion to DCO-cleared, anonymously SEF or DCM-executed swaps in which neither counterparty is subsequently disclosed through the practice of post-trade name give-up. Additionally, Better Markets objected to the expansion of the exchange-trading exclusion for any swaps anonymously executed or cleared through an exempted intermediary.

Having considered these comments, the Commission is adopting this exception as proposed.[292] When a non-U.S. person enters into a swap that is executed anonymously on a registered or exempt SEF, DCM, or registered FBOT, the Commission recognizes that the non-U.S. person does not have the necessary information about its counterparty to determine whether the swap should be included in its SD de minimis threshold calculation. The Commission therefore has determined that in this case the swap should be excluded altogether due to these practical difficulties.[293] However, the exception is limited to Other Non-U.S. Persons since, as discussed, Guaranteed Entities and SRSs have to count all of their dealing swaps towards the threshold, so the practical obstacles that would challenge Other Non-U.S. Persons are not relevant for Guaranteed Entities and SRSs.

The Final Rule expands the exception as it appeared in the Guidance to include SEFs and DCOs that are exempt from registration under the CEA, and also states that SRSs do not qualify for this exception. The CEA provides that the Commission may grant an exemption from registration if it finds that a foreign SEF or DCO is subject to comparable, comprehensive supervision and regulation by the appropriate governmental authorities in the SEF or DCO's home country.[294] The Commission believes that the policy rationale for providing relief to swaps anonymously executed on a SEF, DCM, or FBOT and then cleared also extends to swaps executed on a foreign SEF and/or cleared through a foreign DCO that has been granted an exemption from registration. As noted, the foreign SEF or DCO is subject to comprehensive regulation that is comparable to that applicable to registered SEFs and DCOs.

The Commission has determined not to expand at this time the exception to allow an Other Non-U.S. Person to exclude swaps executed anonymously on an exchange and which are subsequently cleared, regardless of whether the exchange and clearing organization are registered or exempt from registration with the Commission. Commenters argued that if the Other Non-U.S. Person's original counterparty was a U.S. person, the Commission's SEF and DCO registration requirements would independently require the trading venue and clearing organization to register with the Commission or obtain an exemption from registration. While guidance from DMO has suggested that this might be the case with respect to SEFs and DCMs,[295] the Commission has not taken a formal position on whether registration of a SEF or DCM is required where a U.S. person participates on the trading facility, and has stated that it will do so in the future.[296] The Commission may consider expanding the exception pending other amendments to the SEF/DCO regulations and registration requirements.

In response to comments that anonymity should not be required, the Commission proposed this exception (and included it in the Guidance) because when a trade is entered into anonymously on an exchange, the non-U.S. person would not have the necessary information about its counterparty to determine whether the swap should be included in its de minimis threshold calculation.[297] Therefore, these practical difficulties justify the exclusion of the swap altogether. However, if the identity of the counterparty is known to be a U.S. person, then the Other Non-U.S. Person should be seen to be participating in the U.S. swap market. Thus, the Commission has determined that such a non-U.S. person should count such swaps towards its de minimis threshold as otherwise required. Where the U.S. person status of a counterparty is known to the non-U.S. person, the Commission sees no reason to treat a cleared swap differently in the cross-border context than such swap is treated in the domestic U.S. context where cleared swaps entered into in a dealing capacity, whether executed anonymously or otherwise, count toward the SD de minimis threshold.

IV. Cross-Border Application of the Major Swap Participant Registration Tests

CEA section 1a(33) defines the term ''major swap participant'' to include persons that are not SDs but that nevertheless pose a high degree of risk to the U.S. financial system by virtue of the ''substantial'' nature of their swap positions.[298] In accordance with the Dodd-Frank Act and CEA section 1a(33)(B), the Commission adopted rules further defining ''major swap participant'' and providing that a person shall not be deemed an MSP unless its swap positions exceed one of several thresholds.[299] The thresholds were designed to take into account default-related credit risk, the risk of multiple market participants failing close in time, and the risk posed by a market participant's swap positions on an aggregate level.[300] The Commission also adopted interpretive guidance stating

[292] Final § 23.23(d).

[293] *See* Proposed Rule, 85 FR at 973. Additionally, as the Commission has clarified in the past, when a non-U.S. person clears a swap through a registered or exempt DCO, such non-U.S. person would not have to include the resulting swap (*i.e.,* the novated swap) in its de minimis threshold calculation. *See, e.g.,* 2016 Proposal, 81 FR at 71957 n.88. A swap that is submitted for clearing is extinguished upon novation and replaced by new swap(s) that result from novation. *See* 17 CFR 39.12(b)(6). *See also* Derivatives Clearing Organization General Provisions and Core Principles, 76 FR 69334, 69361 (Nov. 8, 2011). Where a swap is created by virtue of novation, such swap does not implicate swap dealing, and therefore it would not be appropriate to include such swaps in determining whether a non-U.S. person should register as an SD.

[294] *See* CEA sections 5h(g) for the SEF exemption provision and 5b(h) for the DCO exemption provision.

[295] Division of Market Oversight Guidance on Application of Certain Commission Regulations to Swap Execution Facilities, at 2 n.8 (Nov. 15, 2013) (''[DMO] expects that a multilateral swaps trading platform located outside the United States that provides U.S. persons . . . with the ability to trade or execute swaps on or pursuant to the rules of the platform, either directly or indirectly through an intermediary, will register as a SEF or DCM.'').

[296] *See* Swap Execution Facilities and Trade Execution Requirement, 83 FR 61946, 61961 n.106 (''[T]he Commission learned that many foreign multilateral swaps trading facilities prohibited U.S. persons and U.S-located persons from accessing their facilities due to the uncertainty that the guidance created with respect to SEF registration. The Commission understands that these prohibitions reflect concerns that U.S. persons and U.S.-located persons accessing their facilities would trigger the SEF registration requirement. . . . [T]he Commission expects to address the application of CEA section 2(i) to foreign multilateral swaps trading facilities, including foreign swaps broking entities, in the future.'').

[297] Proposed Rule, 85 FR at 973; Guidance, 78 FR 45325.

[298] 7 U.S.C. 1a(33)(A) (defining ''major swap participant'' to mean any person that is not an SD and either: (1) Maintains a substantial position in swaps for any of the major swap categories, subject to certain exclusions; (2) whose outstanding swaps create substantial counterparty exposure that could have serious effects on the U.S. financial system; or (3) is a highly leveraged financial entity that is not subject to prudential capital requirements and that maintains a substantial position in swaps for any of the major swap categories).

[299] 17 CFR 1.3, Major swap participant, paragraph (1). *See generally* Entities Rule, 77 FR 30596.

[300] Entities Rule, 77 FR at 30666 (discussing the guiding principles behind the Commission's definition of ''substantial position'' in 17 CFR 1.3); *id.* at 30683 (noting that the Commission's definition of ''substantial counterparty exposure'' in 17 CFR 1.3 is founded on similar principles as its definition of ''substantial position'').

that, for purposes of the MSP analysis, an entity's swap positions are attributable to a parent, other affiliate, or guarantor to the extent that the counterparty has recourse to the parent, other affiliate, or guarantor and the parent or guarantor is not subject to capital regulation by the Commission, SEC, or a prudential regulator (''attribution requirement'').[301]

The Commission is now adopting rules to address the cross-border application of the MSP thresholds to the swap positions of U.S. and non-U.S. persons.[302] Applying CEA section 2(i) and principles of international comity, the Final Rule identifies when a potential MSP's cross-border swap positions apply toward the MSP thresholds and when they may be properly excluded. As discussed below, whether a potential MSP includes a particular swap in its MSP threshold calculations depends on how the entity and its counterparty are classified (*e.g.,* U.S. person, SRS, etc.) and, in some cases, the jurisdiction in which a non-U.S. person is regulated.[303] The Final Rule's approach for the cross-border application of the MSP thresholds is similar to the approach described above for the SD threshold.

A. U.S. Persons

The Commission is adopting, as proposed, the requirement that a U.S. person include all of its swap positions in its MSP registration threshold calculations without exception.[304] The Commission did not receive comments regarding this requirement. As discussed in the context of the Final Rule's approach to applying the SD de minimis registration threshold, by virtue of it being domiciled or organized in the United States, or the inherent nature of its connection to the United States, all of a U.S. person's activities have a significant nexus to U.S. markets, giving the Commission a particularly strong regulatory interest in its swap activities.[305] Accordingly, the Commission believes that all of a U.S. person's swap positions, regardless of where they occur or the U.S. person status of the counterparty, should apply toward the MSP thresholds.

B. Non-U.S. Persons

Under the Final Rule, as discussed in more detail below, whether a non-U.S. person includes a swap position in its MSP threshold calculations depends on its status, the status of its counterparty, or the characteristics of the swap. Specifically, the Final Rule requires a person that is a Guaranteed Entity or an SRS to count all of its swap positions. In addition, an Other Non-U.S. Person is required to count all swap positions with a U.S. person, except for swaps conducted through a foreign branch of a registered U.S. SD. Subject to an exception, the Final Rule also requires an Other Non-U.S. Person to count all swap positions if the counterparty to such swaps is a Guaranteed Entity.[306]

1. Swaps by a Significant Risk Subsidiary

The Commission proposed to require an SRS to include all of its swap positions in its MSP threshold calculations.[307]

IIB/SIFMA recommended that the Commission not adopt the proposal, asserting that absent a guarantee or other form of direct risk transfer to a U.S. person, a foreign subsidiary does not present sufficiently ''direct'' risk to the United States to justify extraterritorial application of the MSP registration requirement under section 2(i). IIB/SIFMA stated that permitting foreign subsidiaries to transact in swaps without registering as MSPs also would not create a substantial regulatory loophole, as there is no evidence of sufficiently substantial non-dealing swap activity occurring in foreign subsidiaries at present when SRSs are not subject to MSP registration (just as there are no U.S. persons currently registered as MSPs).

After considering the comment, the Commission is adopting this aspect of the cross-border application of the MSP registration thresholds as proposed.[308] As noted in section II.D, the term SRS encompasses a person that, by virtue of being a significant subsidiary of a U.S. person, and not being subject to prudential supervision as a subsidiary of a BHC or IHC or subject to comparable capital and margin rules, raises the concerns intended to be addressed by the Dodd-Frank Act requirements addressed by the Final Rule, regardless of the U.S. person status of its counterparty. Further, the Commission believes that treating an SRS differently from a U.S. person could create a substantial regulatory loophole by incentivizing U.S. persons to conduct their swap business with non-U.S. persons through SRSs to avoid application of the Dodd-Frank Act MSP requirements. Allowing swaps entered into by SRSs, which have the potential to affect the ultimate U.S. parent entity and U.S. commerce, to be treated differently depending on how the parties structure their transactions could undermine the effectiveness of the Dodd-Frank Act swap provisions and related Commission regulations addressed by the Final Rule. Applying the same standard to similar swap positions helps to limit those incentives and regulatory implications.[309] Additionally, the SRS definition already includes a carve-out for affiliates of U.S. BHCs and IHCs. This approach allows for streamlined application of the rule, and the comment letters have not identified specific problems caused by applying the same standard to similar swap positions.

In addition, a person's status as an SRS is determined at the entity level and, thus, an SRS is required to include in its MSP threshold calculations the swap positions of its operations that are part of the same legal person, including those of its branches.[310]

For added clarity, the Commission also notes that an Other Non-U.S. Person is not be required to include swap positions entered into with an SRS in its MSP threshold calculations, unless the SRS is also a Guaranteed Entity and no other exception applies.

2. Swap Positions With a U.S. Person

The Commission proposed to require an Other Non-U.S. Person to count toward its MSP registration thresholds swap positions where the counterparty is a U.S. person, other than swaps with a foreign branch of a registered U.S. SD if such swaps are conducted through a foreign branch of such registered SD.[311]

IIB/SIFMA supported this approach, stating that it is consistent with the Guidance, except that it does not require that swaps with a foreign branch of a registered SD be subject to daily variation margin in order to be excluded from an Other Non-U.S. Person's MSP

[301] *Id.* at 30689.

[302] Final § 23.23(c).

[303] As indicated above, for purposes of the Final Rule, an ''Other Non-U.S. Person'' refers to a non-U.S. person that is neither a Guaranteed Entity nor an SRS.

[304] Final § 23.23(c)(1); Proposed Rule, 85 FR at 974, 1004.

[305] *See supra* section III.A; Proposed Rule, 85 FR at 974.

[306] As discussed in sections II.C and III.B, *supra,* for purposes of this release and ease of reading, such a non-U.S. person whose obligations under the swaps are subject to a guarantee by a U.S. person is being referred to as a ''Guaranteed Entity.'' Depending on the characteristics of the swap, a non-U.S. person may be a Guaranteed Entity with respect to swaps with certain counterparties, but not be deemed a Guaranteed Entity with respect to swaps with other counterparties.

[307] Proposed § 23.23(c)(1); Proposed Rule, 85 FR at 974–975, 1004.

[308] Final § 23.23(c)(1).

[309] Proposed Rule, 85 FR at 974–975.

[310] *Id.*

[311] Proposed § 23.23(c)(2)(i); Proposed Rule, 85 FR at 975, 1004.

registration thresholds. IIB/SIFMA noted that this was appropriate because the Dodd-Frank Act's margin requirements independently impose variation margin requirements on SDs where appropriate. Further, they stated that the change removes the complexity of non-U.S. persons having to determine their own ''financial entity'' status in order to evaluate whether variation margin was required now that the uncleared swap margin rules use a slightly different ''financial end user'' definition.

After considering this comment, the Commission is adopting this aspect of the cross-border application of the MSP registration thresholds as proposed.[312] Generally, a potential MSP must include in its MSP threshold calculations any swap position with a U.S. person. As discussed above, the term ''U.S. person'' encompasses persons that inherently raise the concerns intended to be addressed by the Dodd-Frank Act, regardless of the U.S. person status of their counterparty. The default or insolvency of the non-U.S. person would have a direct and significant adverse effect on a U.S. person and, by virtue of the U.S. person's significant nexus to the U.S. financial system, potentially could result in adverse effects or disruption to the U.S. financial system as a whole, particularly if the non-U.S. person's swap positions are substantial enough to exceed an MSP registration threshold.[313]

The Final Rule's approach in allowing a non-U.S. person to exclude swap positions conducted through a foreign branch of a registered SD counterparty is consistent with the approach described in section III.B.2 for cross-border treatment with respect to SDs.[314] In this regard, a swap conducted through a foreign branch of a registered SD triggers certain Dodd-Frank Act transactional requirements (or comparable requirements), particularly margin requirements, and therefore mitigates concern that this exclusion could be used to engage in swap activities outside the Dodd-Frank Act regime.

Accordingly, the Commission has determined that it is appropriate and consistent with section 2(i) of the CEA to allow a non-U.S. person, which is not a Guaranteed Entity or SRS, to exclude from its MSP threshold calculations any swaps conducted through a foreign branch of a registered SD counterparty. The Commission recognizes that the Guidance provided that such swaps would need to be cleared or that the documentation of the swaps would have to require the foreign branch to collect daily variation margin, with no threshold, on its swaps with such non-U.S. person.[315] The Final Rule does not include such a requirement because the foreign branch of the registered SD is nevertheless required to post and collect margin, as required by the SD margin rules. In addition, a non-U.S. person's swaps conducted through a foreign branch of a registered SD counterparty must be addressed in the SD's risk management program. Such program must account for, among other things, overall credit exposures to non-U.S. persons.[316]

In response to a request for comment,[317] IIB/SIFMA supported not requiring a U.S. branch of a non-U.S. banking organization to include all of its swap positions in its MSP calculation as if they were swaps entered into by a U.S. person or to require an Other Non-U.S. Person to include in its MSP calculation dealing swaps conducted through such a branch. IIB/SIFMA stated that swaps between a U.S. branch and an Other Non-U.S. Person do not present risks to the United States that would justify applying the Commission's MSP requirements. Consistent with the Proposed Rule, the Commission has determined not to require a U.S. branch to include swaps with Other Non-U.S. Persons in its MSP threshold calculations as if they were swaps entered into by a U.S. person. Similarly, the Final Rule does not require an Other Non-U.S. Person to include in its MSP calculation dealing swaps booked in a U.S. branch.

3. Guaranteed Swap Positions

(i) Swap Positions Entered Into by a Guaranteed Entity

The Commission proposed to require a non-U.S. person to include in its MSP calculation each swap position with respect to which it is a Guaranteed Entity.[318] No comments were received regarding this aspect of the Proposed Rule, and the Commission is adopting this aspect of the cross-border application of the MSP registration thresholds as proposed.[319]

As explained in the context of the SD de minimis threshold calculation, the Commission believes that the swap positions of a Guaranteed Entity are identical, in relevant aspects, to those entered into directly by a U.S. person and thus present similar risks to the stability of the U.S. financial system or of U.S. entities.[320] As a result of the guarantee, the U.S. guarantor generally bears risk arising out of the swap as if it had entered into the swap directly. Absent the guarantee from the U.S. person, a counterparty may choose not to enter into the swap or may not do so on the same terms. Treating Guaranteed Entities differently from U.S. persons could also create a substantial regulatory loophole, allowing transactions that have a similar connection to or effect on U.S. commerce to be treated differently depending on how the parties are structured and thereby undermining the effectiveness of the Dodd-Frank Act swap provisions and related Commission regulations.

(ii) Swaps Positions Entered Into With a Guaranteed Entity

The Commission also proposed to require an Other Non-U.S. Person to count toward its MSP registration thresholds swap positions with a counterparty that is a Guaranteed Entity, except when the counterparty is registered as an SD.[321]

IIB/SIFMA supported this approach, stating that it is consistent with the Guidance, except that it does not require that swaps with a Guaranteed Entity be subject to daily variation margin in order to be excluded from an Other Non-U.S. Person's MSP registration thresholds. IIB/SIFMA noted that this was appropriate because the Dodd-Frank Act's margin requirements independently impose variation margin requirements on SDs where appropriate. Further, they stated that the change removes the complexity of non-U.S. persons having to determine their own ''financial entity'' status in order to evaluate whether variation margin was required now that the uncleared swap margin rules use a slightly different ''financial end user'' definition.

The Commission is adopting as proposed the requirement that a non-U.S. person must count swap positions

[312] Final § 23.23(c)(2)(i).

[313] Proposed Rule, 85 FR at 975.

[314] *Id.*

[315] Guidance, 78 FR at 45324–45325.

[316] *See* 17 CFR 23.600(c)(4)(ii), requiring registered SDs and MSPs to have credit risk policies and procedures that account for daily measurement of overall credit exposure to comply with counterparty credit limits, and monitoring and reporting of violations of counterparty credit limits performed by personnel that are independent of the business trading unit. *See also* 17 CFR 23.600(c)(1)(i), requiring the senior management and the governing body of each SD and MSP to review and approve credit risk tolerance limits for the SD or MSP.

[317] Proposed Rule, 85 FR at 977.

[318] Proposed § 23.23(c)(2)(ii); Proposed Rule, 85 FR at 975, 1004.

[319] Final § 23.23(c)(2)(ii).

[320] *See supra* section III.B.3.i; Proposed Rule, 85 FR at 975.

[321] Proposed § 23.23(c)(2)(iii); Proposed Rule, 85 FR at 975–976, 1004.

with a Guaranteed Entity counterparty, except when the counterparty is registered as an SD.[322] The guarantee of a swap is an integral part of the swap and, as discussed above, counterparties may not be willing to enter into a swap with a Guaranteed Entity in the absence of the guarantee. The Commission also recognizes that, given the highly integrated corporate structures of global financial enterprises, financial groups may elect to conduct their swap activity in a number of different ways, including through a U.S. person or through a non-U.S. affiliate that benefits from a guarantee from a U.S. person. Therefore, in order to avoid creating a substantial regulatory loophole, the Commission has determined that swap positions of a non-U.S. person with a counterparty whose obligations under the swaps are guaranteed by a U.S. person must receive the same treatment as swap positions with a U.S. person.[323]

However, similar to the discussion regarding SDs in section III.B.3.ii, where an Other Non-U.S. Person enters into a swap with a Guaranteed Entity that is a registered SD, it is appropriate to permit the non-U.S. person not to count its swap position with the Guaranteed Entity against the non-U.S. person's MSP thresholds, because one counterparty to the swap is a registered SD subject to comprehensive swap regulation and operating under the oversight of the Commission. For example, the swap position must be addressed in the SD's risk management program and account for, among other things, overall credit exposures to non-U.S. persons.[324] In addition, a non-U.S. person's swap positions with a Guaranteed Entity that is an SD are included in exposure calculations and attributed to the U.S. guarantor for purposes of determining whether the U.S. guarantor's swap exposures are systemically important on a portfolio basis and therefore require the protections provided by MSP registration. Therefore, in these circumstances, the Commission has determined that the non-U.S. person need not count such a swap position toward its MSP thresholds.[325]

C. Attribution Requirement

In the Entities Rule, the Commission and the SEC provided a joint interpretation that an entity's swap positions in general are attributed to a parent, other affiliate, or guarantor for purposes of the MSP analysis to the extent that the counterparties to those positions have recourse to the parent, other affiliate, or guarantor in connection with the position, such that no attribution is required in the absence of recourse.[326] Even in the presence of recourse, however, attribution of a person's swap positions to a parent, other affiliate, or guarantor is not necessary if the person is already subject to capital regulation by the Commission or the SEC or is a U.S. entity regulated as a bank in the United States (and is therefore subject to capital regulation by a prudential regulator).[327]

The Commission proposed to address the cross-border application of the attribution requirement in a manner consistent with the Entities Rule and CEA section 2(i) and generally comparable to the approach adopted by the SEC.[328] Specifically, the Commission stated that the swap positions of an entity, whether a U.S. or non-U.S. person, should not be attributed to a parent, other affiliate, or guarantor for purposes of the MSP analysis in the absence of a guarantee. The Commission stated that even in the presence of a guarantee, attribution would not be required if the entity that entered into the swap directly is subject to capital regulation by the Commission or the SEC or is regulated as a bank in the United States.[329] Additionally, the Commission invited comment on whether it should modify its interpretation with regard to the attribution requirement to provide that attribution of a person's swap positions to a parent, other affiliate, or guarantor would not be required if the person is subject to capital standards that are comparable to and as comprehensive as the capital regulations and oversight by the Commission, SEC, or a U.S. prudential regulator.[330]

IIB/SIFMA stated that the Guidance clarified that the exception for entities subject to capital regulation also includes entities subject to non-U.S. capital standards that are comparable to, and as comprehensive as, the capital regulations and oversight by the Commission, SEC, or a U.S. prudential regulator (*i.e.,* Basel compliant capital standards and oversight by a G20 prudential supervisor). Therefore, IIB/SIFMA recommended that the attribution requirement in the MSP threshold context should exclude entities subject to Basel compliant capital standards and oversight by a G20 prudential supervisor, as those entities should pose no higher risk than entities subject to capital regulation by the Commission, SEC, or a prudential regulator.

The Commission is adopting the interpretation of the attribution requirement as discussed in the Proposed Rule, with a clarification. The Commission has determined that, in addition to entities that are subject to capital regulation by the Commission, SEC, or U.S. prudential regulators, the attribution requirement in the MSP threshold context also excludes entities subject to Basel compliant capital standards and oversight by a G20 prudential supervisor. As noted by IIB/SIFMA in response to a request for comment, this approach is consistent with the Guidance, and is recommended because those entities pose no higher risk than entities subject to capital regulation by the Commission, SEC, or a prudential regulator. The Commission has further determined that the swap positions of an entity that is required to register as an MSP, or whose MSP registration is pending, are not subject to the attribution requirement.

Generally, if a guarantee is present, however, and the entity being guaranteed is not subject to capital regulation (as described above), whether the attribution requirement applies depends on the U.S. person status of the person to whom there is recourse under the guarantee (*i.e.,* the U.S. person status of the guarantor). Specifically, a U.S. person guarantor attributes to itself any swap position of an entity subject to a guarantee, whether a U.S. person or a non-U.S. person, for which the counterparty to the swap has recourse against that U.S. person guarantor. The Commission finds that when a U.S. person acts as a guarantor of a swap position, the guarantee creates risk within the United States of the type that MSP regulation is intended to address, regardless of the U.S. person status of the entity subject to a guarantee or its counterparty.[331]

A non-U.S. person attributes to itself any swap position of an entity for which the counterparty to the swap has

[322] Final § 23.23(c)(2)(iii). The MSP provision does not include an exception for swap positions with non-U.S. persons guaranteed by a non-financial entity, or for swap positions with a Guaranteed Entity where such Guaranteed Entity is itself below the SD de minimis threshold under paragraph (4)(i) of the "swap dealer" definition in § 1.3 and is affiliated with a registered SD, similar to the carve-outs in the SD provision. *See* Final § 23.23(b)(2)(iii)(B) and (C); *supra* section III.B.3.ii.

[323] Proposed Rule, 85 FR at 975–976.

[324] *See* 17 CFR 23.600(c)(4)(ii). *See also* 17 CFR 23.600(c)(1)(i).

[325] Proposed Rule, 85 FR at 975–976.

[326] Entities Rule, 77 FR at 30689.

[327] *Id.*

[328] Proposed Rule, 85 FR at 976. *See* SEC Cross-Border Rule, 79 FR at 47346–47348.

[329] Proposed Rule, 85 FR at 976.

[330] *Id.* at 977.

[331] *Id.* at 976. *See* Entities Rule, 77 FR at 30689 (attribution is intended to reflect the risk posed to the U.S. financial system when a counterparty to a position has recourse against a U.S. person).

recourse against the non-U.S. person unless all relevant persons (*i.e.,* the non-U.S. person guarantor, the entity whose swap positions are guaranteed, and its counterparty) are non-U.S. persons that are not Guaranteed Entities.[332] In this regard, the Commission finds that when a non-U.S. person provides a guarantee with respect to the swap position of a particular entity, the economic reality of the swap position is substantially identical, in relevant respects, to a position entered into directly by the non-U.S. person.

In addition, the Commission believes that entities subject to a guarantee are able to enter into significantly more swap positions (and take on significantly more risk) as a result of the guarantee than they can otherwise, amplifying the risk of the non-U.S. person guarantor's inability to carry out its obligations under the guarantee. Given the types of risk that MSP regulation is intended to address, the Commission has a strong regulatory interest in ensuring that the attribution requirement applies to non-U.S. persons that provide guarantees to U.S. persons and Guaranteed Entities. Accordingly, the Commission has determined that a non-U.S. person must attribute to itself the swap positions of any entity for which it provides a guarantee unless it, the entity subject to the guarantee, and its counterparty are all non-U.S. persons that are not Guaranteed Entities.

D. Certain Exchange-Traded and Cleared Swaps

Consistent with its approach for SDs, the Commission proposed to allow a non-U.S. person that is not a Guaranteed Entity or an SRS to exclude from its MSP calculation any swap position that it anonymously enters into on a DCM, a registered SEF or a SEF exempted from registration by the Commission pursuant to section 5h(g) of the CEA, or an FBOT registered with the Commission pursuant to part 48 of its regulations,[333] if such swap is also cleared through a registered or exempt DCO.[334]

As discussed in section III.D in connection with the cross-border application of the SD registration threshold, as compared to the Proposed Rule, IIB/SIFMA, JFMC/IBAJ, JBA, and JSCC advocated for expansion of this exception, while Better Markets stated that the proposed exception should be narrowed.

Consistent with the cross-border application of the SD registration threshold, the Commission is adopting this exception as proposed.[335] When a non-U.S. person enters into a swap position that is executed anonymously on a registered or exempt SEF, DCM, or registered FBOT, the Commission recognizes that the non-U.S. person does not have the necessary information about its counterparty to determine whether the swap position should be included in its MSP calculation. The Commission has determined that in this case the swap position should be excluded altogether due to these practical difficulties.[336] However, the exception is limited to Other Non-U.S. Persons since, as discussed, Guaranteed Entities and SRSs have to count all of their swap positions towards the threshold, so the practical obstacles that would challenge Other Non-U.S. Persons are not relevant for Guaranteed Entities and SRSs.

The Final Rule expands the exception as it appeared in the Guidance to include SEFs and DCOs that are exempt from registration under the CEA, and also states that SRSs do not qualify for this exception. The CEA provides that the Commission may grant an exemption from registration if it finds that a foreign SEF or DCO is subject to comparable, comprehensive supervision and regulation by the appropriate governmental authorities in the SEF or DCO's home country.[337] The policy rationale for providing relief to swap positions anonymously executed on a SEF, DCM, or FBOT and then cleared also extends to swaps executed on a foreign SEF and/or cleared through a foreign DCO that has been granted an exemption from registration. As noted, the foreign SEF or DCO is subject to comprehensive regulation that is comparable to that applicable to registered SEFs and DCOs.

The Commission is not at this time expanding the exception to allow an Other Non-U.S. Person to exclude swap positions executed anonymously on an exchange and which are subsequently cleared, regardless of whether the exchange and clearing organization are registered or exempt from registration with the Commission. Commenters argued that if the Other Non-U.S. Person's original counterparty was a U.S. person, the Commission's SEF and DCO registration requirements would independently require the trading venue and clearing organization to register with the Commission or obtain an exemption from registration. While guidance from DMO has suggested that this might be the case with respect to SEFs and DCMs,[338] the Commission has not taken a formal position on whether registration of a SEF or DCM is required where a U.S. person participates on the trading facility, and has stated that it will do so in the future.[339] The Commission may consider expanding the exception pending other amendments to the SEF/DCO regulations.

In response to comments that anonymity should not be required, the Commission proposed this exception (and included it in the Guidance) because when a trade is entered into anonymously on an exchange, the non-U.S. person would not have the necessary information about its counterparty to determine whether the swap position should be included in its MSP calculation.[340] Therefore, these practical difficulties justify exclusion of the swap position altogether. However, if the identity of the counterparty is known to be a U.S. person, then the Other Non-U.S. Person should be seen to be participating in the U.S. swap market. Thus, the Commission has determined that such a non-U.S. person should count such swap positions towards its MSP calculation as otherwise required. As stated above, where the U.S. person status of a counterparty is known to the non-U.S. person, the Commission sees no reason to treat a cleared swap differently in the cross-border context than such swap

[332] As noted above, the term Guaranteed Entity is limited to entities that are guaranteed by a U.S. person.

[333] The Commission considers the exception described herein also to apply with respect to an FBOT that provides direct access to its order entry and trade matching system from within the U.S. pursuant to no-action relief issued by Commission staff.

[334] Proposed § 23.23(d); Proposed Rule, 85 FR at 976, 1004.

[335] Final § 23.23(d).

[336] *See* Proposed Rule, 85 FR at 976.

[337] *See* CEA sections 5h(g) for the SEF exemption provision and 5b(h) for the DCO exemption provision.

[338] Division of Market Oversight Guidance on Application of Certain Commission Regulations to Swap Execution Facilities, at 2 n.8 (Nov. 15, 2013) (''[DMO] expects that a multilateral swaps trading platform located outside the United States that provides U.S. persons . . . with the ability to trade or execute swaps on or pursuant to the rules of the platform, either directly or indirectly through an intermediary, will register as a SEF or DCM.'').

[339] *See* Swap Execution Facilities and Trade Execution Requirement, 83 FR 61946, 61961 n.106 (''[T]he Commission learned that many foreign multilateral swaps trading facilities prohibited U.S. persons and U.S-located persons from accessing their facilities due to the uncertainty that the guidance created with respect to SEF registration. The Commission understands that these prohibitions reflect concerns that U.S. persons and U.S.-located persons accessing their facilities would trigger the SEF registration requirement. . . . [T]he Commission expects to address the application of CEA section 2(i) to foreign multilateral swaps trading facilities, including foreign swaps broking entities, in the future.'').

[340] Proposed Rule, 85 FR at 976; Guidance, 78 FR 45325.

position is treated in the domestic U.S. context.

V. ANE Transactions

A. Background and Proposed Approach

The ANE Staff Advisory provided that a non-U.S. SD would generally be required to comply with Transaction-Level Requirements (as that term was used in the Guidance) when entering into ANE Transactions.[341]

In the Proposed Rule the Commission stated that, based on the Commission's consideration of its experience under the Guidance, the comments it had received pursuant to the ANE Request for Comment,[342] respect for international comity, and the Commission's desire to focus its authority on potential significant risks to the U.S. financial system, the Commission had determined that ANE Transactions will not be considered a relevant factor for purposes of applying the Proposed Rule.[343] Therefore, under the Proposed Rule, all foreign-based swaps entered into between a non-U.S. swap entity and a non-U.S. person would be treated the same regardless of whether the swap is an ANE Transaction. The Commission further noted that, to the extent the Proposed Rule is finalized, this treatment would effectively supersede the ANE Staff Advisory with respect to the application of the group B and C requirements (discussed in sections VI.A.2 and VI.A.3 below) to ANE Transactions.

With respect to its experience, the Commission noted that the ANE No-Action Relief, which went into effect immediately after issuance of the ANE Staff Advisory, generally relieved non-U.S. swap entities from the obligation to comply with most Transaction-Level Requirements when entering into swaps with most non-U.S. persons.[344] The Commission also noted that in the intervening period, the Commission had not found a negative effect on either its ability to effectively oversee non-U.S. swap entities, or the integrity and transparency of U.S. derivatives markets.

Noting its interest in international comity, the Commission observed that ANE Transactions involve swaps between non-U.S. persons, and thus the Commission considered whether the U.S. aspect of ANE Transactions should override its general view that such transactions should qualify for the same relief provided under the Proposed Rule (and the Guidance) for swaps between certain non-U.S. persons (*e.g.,* an exception from compliance with Transaction-Level Requirements under the Guidance and group B and C requirements under the Proposed Rule, as discussed below). The Commission expressly recognized that a person that, in connection with its dealing activity, engages in market-facing activity using personnel located in the United States is conducting a substantial aspect of its dealing business in the United States. But, because the transactions involve two non-U.S. persons, and the financial risk of the transactions lies outside the United States, the Commission considered the extent to which the underlying regulatory objectives of the Dodd-Frank Act would be advanced in light of other policy considerations, including undue market distortions and international comity, when making a determination of the extent to which the Dodd-Frank Act swap requirements would apply to ANE Transactions.

The Commission noted that the consequences of not applying the Dodd-Frank Act swap requirements would be mitigated in two respects. First, persons engaging in any aspect of swap transactions within the U.S. remain subject to the CEA and Commission regulations prohibiting the employment, or attempted employment, of manipulative, fraudulent, or deceptive devices, such as section 6(c)(1) of the CEA,[345] and § 180.1.[346] The Commission thus would retain anti-fraud and anti-manipulation authority, and would continue to monitor the trading practices of non-U.S. persons that occur within the territory of the United States in order to enforce a high standard of customer protection and market integrity. Even where a swap is entered into by two non-U.S. persons, the United States has a significant interest in deterring fraudulent or manipulative conduct occurring within its borders and cannot be a haven for such activity.

Second, with respect to more specific regulation of swap dealing in accordance with the Commission's swap regime, the Commission noted that, in most cases, non-U.S. persons entering into ANE Transactions would be subject to regulation and oversight in their home jurisdictions similar to the Commission's Transaction-Level Requirements as most of the major swap trading centers have implemented similar risk mitigation requirements.[347]

With respect to market distortion, the Commission gave weight to comments submitted in response to the ANE Request for Comment, who argued that application of Transaction-Level Requirements to ANE Transactions would cause non-U.S. SDs to relocate personnel to other countries (or otherwise terminate agency contracts with U.S.-based agents) in order to avoid Dodd-Frank Act swap regulation or to have to interpret and apply what the commenters considered a challenging ANE analysis, thereby potentially increasing market fragmentation.[348]

The Commission also gave weight to the regulatory interests of the home jurisdictions of non-U.S. persons engaged in ANE Transactions. Because the risk of the resulting swaps lies in those home countries and not the U.S. financial system, the Commission recognized that, with the exception of enforcing the prohibition on fraudulent or manipulative conduct taking place in the United States, non-U.S. regulators will have a greater incentive to regulate the swap dealing activities of such non-U.S. persons—such as, for example, with respect to business conduct standards with counterparties, appropriate documentation, and recordkeeping. In these circumstances, where the risk lies outside the U.S. financial system, the Commission recognized the greater supervisory interest of the authorities in the home jurisdictions of the non-U.S. persons. The Commission also noted that no major swap regulatory jurisdiction applies its regulatory regime to U.S. entities engaging in ANE Transactions within its territory.

In light of the foregoing, the Commission determined that the mitigating effect of the anti-fraud and anti-manipulation authority retained by

[341] *See* ANE Staff Advisory. The ANE Staff Advisory represented the views of DSIO only, and not necessarily those of the Commission or any other office or division thereof. As discussed in section VI.A, *infra,* the Transaction-Level Requirements are: (1) Required clearing and swap processing; (2) margining (and segregation) for uncleared swaps; (3) mandatory trade execution; (4) swap trading relationship documentation; (5) portfolio reconciliation and compression; (6) real-time public reporting; (7) trade confirmation; (8) daily trading records; and (9) external business conduct standards.

[342] In the January 2014 ANE Request for Comment, the Commission requested comments on all aspects of the ANE Staff Advisory, including: (1) The scope and meaning of the phrase ''regularly arranging, negotiating, or executing'' and what characteristics or factors distinguish ''core, front-office'' activity from other activities; and (2) whether the Commission should adopt the ANE Staff Advisory as Commission policy, in whole or in part.

[343] *See* Proposed Rule, 85 FR at 977–979.

[344] Specifically, non-U.S. persons that are neither guaranteed nor conduit affiliates, as described in the Guidance.

[345] 7 U.S.C. 9(1).

[346] 17 CFR 180.1.

[347] *See* 2019 FSB Progress Report, Table M.

[348] Proposed Rule, 85 FR at 977.

the Commission and the prevalence of applicable regulatory requirements similar to the Commission's own, the likelihood of market fragmentation and disruption, the Commission's respect for the regulatory interests of the foreign jurisdictions where the actual financial risks of ANE Transactions primarily lie in accordance with the principles of international comity, and the awareness that application of its swap requirements in the ANE context would make the Commission an outlier among the major swap regulatory jurisdictions, outweighed the Commission's regulatory interest in applying its swap requirements to ANE Transactions differently than such were otherwise proposed to be applied to swaps between Other Non-U.S. Persons. The Commission invited comment on all aspects of the proposed treatment of ANE Transactions.

B. Summary of Comments

Neither Better Markets nor AFR supported the Commission's determination to disregard ANE Transactions and commented that the Commission should not permit U.S.-located personnel to arrange, negotiate, or execute swaps on behalf of the non-U.S. affiliates of U.S. BHCs (and others) without being subject to the full panoply of U.S. regulations. Better Markets stated its belief that any such policy facilitates avoidance, if not evasion, and regulatory arbitrage. Better Markets specifically disputed the Commission's contention in the Proposed Rule that ''the financial risk of the [ANE] transactions [only] lie outside of the United States,'' which Better Markets contends is demonstrably untrue and conflicts with the Commission's own views elsewhere in the Proposed Rule, presumably referring to the proposed treatment of swaps of non-U.S. persons with Guaranteed Entities and SRSs, which are also non-U.S. persons that the Commission nevertheless proposed generally would be subject to certain Dodd-Frank Act requirements.[349]

On the other hand, AIMA, Chatham Financial, CS, IIB/SIFMA, ISDA, and JFMC/IBAJ supported the Commission's decision in the Proposed Rule to only apply anti-fraud and anti-manipulation rules to ANE Transactions, agreeing in various respects with the Commission's analysis that:

1. ANE Transactions do not present direct financial risk to the United States;
2. The Commission's anti-fraud and anti-manipulation rules that would remain applicable would mitigate potential concerns associated with any potential misconduct occurring in connection with ANE Transactions and any other conduct subject to the jurisdiction of the CEA;
3. Most ANE Transactions are expected to be subject to foreign regulatory requirements similar to the Commission's own, unlike at the time of the adoption of the Guidance; and
4. Applying the Commission's rules to ANE Transactions would likely result in disruptive and unnecessary market fragmentation as transactions ordinarily arranged, negotiated, or executed by U.S. personnel would shift to non-U.S. locations, resulting in decreased Commission oversight.

Commenting on specific aspects of the Commission's proposed treatment of ANE Transactions, AIMA encouraged the CFTC to adopt the SEC's approach and require counting of ANE Transactions toward the SD registration threshold and to apply reporting requirements to ensure that a baseline level of transparency is maintained.

IIB/SIFMA recognized that the Proposed Rule's approach to ANE Transactions would deviate from that taken by the SEC, but argued that this deviation is justified. They argued that the relationship of the security-based swap market to the cash securities markets, and Congress's decision to define security-based swaps as ''securities,'' presents some justification for the SEC to apply a test for use of U.S. jurisdictional means to conduct security-based swap business that is similar to the test that applies in connection with existing, pre-Dodd-Frank Act securities broker-dealer regulation, while no similar justification applies in connection with swaps regulation by the Commission, as the swaps market generally trades independently of the U.S. futures market, and Congress did not define swaps to be a type of futures contract.

IIB/SIFMA, CS, JFMC/IBAJ, and ISDA also commented on the continuing viability of the ANE Staff Advisory. These commenters stated that, currently, ANE Transactions are subject to the ANE Staff Advisory and related ANE No-Action Relief, noting that, if adopted, the Proposed Rule would supersede the ANE Staff Advisory, but only with respect to those requirements covered by the Proposed Rule. These commenters noted that certain other Commission requirements—mandatory clearing, mandatory trade execution, and real-time public reporting—would remain subject to the ANE Staff Advisory and related ANE No-Action Relief, pending further Commission action. To achieve a coherent, Commission-driven ANE Transaction policy, these commenters all requested that the Commission immediately direct staff to withdraw the ANE Staff Advisory (which, in their view, would render the ANE No-Action Relief moot).

ISDA noted that the ANE No-Action Relief was issued two weeks after the ANE Staff Advisory and that market participants have operated under this relief for almost seven years. ISDA argued that, during this time, to ISDA's knowledge, there have been no regulatory concerns associated with these transactions that would warrant a change in course. Thus, should the Commission decide to switch gears and apply clearing, trading, and real-time reporting requirements to ANE Transactions, market participants would incur significant compliance costs without commensurate benefit to the Commission's regulatory oversight.

Although Citadel agreed that the Commission should apply its jurisdiction over ANE Transactions in a targeted manner, taking into account principles of international comity, as well as its supervisory interests and statutory objectives, Citadel argued that because the Commission's relevant statutory objectives include not only mitigating systemic risk, but also increasing transparency, competition, and market integrity, the Commission should, at a minimum, apply regulatory and public reporting requirements to ANE Transactions. AIMA also encouraged the Commission to apply reporting requirements to ensure that a baseline level of transparency is maintained. Citadel stated that application of reporting requirements to these transactions would enable the Commission to better monitor for disruptive trading practices and provide the necessary data regarding overall market trading activity to allow the Commission to evaluate market trends and accurately assess the effect of other reforms implemented in the swaps market.

Stating that ANE Transactions could account for a material portion of total swap dealing activity in the United States, Citadel claimed that market transparency in EUR interest rate swaps for U.S. investors has been greatly reduced based on data showing that, following issuance of the ANE No-Action Relief, interdealer trading activity in EUR interest rate swaps

[349] As discussed below, the Final Rule excepts certain transactions with ''SRS End-Users'' from the Group B requirements, excepts certain transactions with Guaranteed Entities and SRSs from the Group C requirements, and provides a limited exception from the Group B requirements for transactions entered into by Guaranteed Entities and SRSs that are swap entities with certain non-U.S. persons. *See infra* sections VI.B.3 and VI.B.5.

began to be booked almost exclusively to non-U.S. entities, a fact pattern that Citadel believes is ''consistent with (although not direct proof of) swap dealers strategically choosing the location of the desk executing a particular trade in order to avoid trading in a more transparent and competitive setting.'' Citadel further noted that applying regulatory and public reporting requirements to ANE Transactions would be consistent with the SEC's approach.

C. Commission Determination

Having considered the comments received, the Commission's consideration of its experience under the Guidance, respect for international comity, and the Commission's desire to focus its authority on potential significant risks to the U.S. financial system, the Commission has determined that, consistent with its rationale expressed in the Proposed Rule summarized above, ANE Transactions will not be considered a relevant factor for purposes of applying the Final Rule.

Regarding the many comments and suggestions received regarding whether the Commission should withdraw the ANE Staff Advisory and related ANE No-Action Relief and extend its proposed treatment of ANE Transactions to requirements in addition to the group B and group C requirements, in 2014, subsequent to the publication of the ANE Staff Advisory, the Commission, citing the complex legal and policy issues raised by the statements in the ANE Staff Advisory, requested comments on whether the Transaction-Level Requirements should apply to swap transactions between certain non-U.S. SDs and non-U.S. counterparties that are ''arranged, negotiated, or executed'' by the SDs' personnel or agents located in the United States.[350] The Commission did not follow-up on the request for comment. In this rulemaking, the Commission is addressing the issue with respect to the group B and group C requirements; the Commission intends to address the issue with respect to the remaining Transaction-Level Requirements (the ''Unaddressed TLRs'') in connection with future cross-border rulemakings relating to such requirements. Until such time, the Commission will not consider, as a matter of policy, a non-U.S. swap entity's use of their personnel or agents located in the United States to ''arrange, negotiate, or execute'' swap transactions with non-U.S. counterparties for purposes of determining whether Unaddressed TLRs apply to such transactions. As part of any such rulemaking, the Commission expects to first engage in fact-finding to determine the extent to which ANE Transactions raise policy concerns that are not otherwise addressed by the CEA or Commission regulations. In this connection, DSIO is withdrawing the ANE Staff Advisory and, together with the Division of Clearing and Risk and DMO, is withdrawing the ANE No-Action Relief and granting certain non-U.S. SDs no-action relief with respect to the applicability of the Unaddressed TLRs to their transactions with non-U.S. counterparties that are arranged, negotiated, or executed in the United States.

The Commission will take AIMA and Citadel's comments regarding the advisability of applying the Commission's regulatory and real-time reporting requirements to ANE Transactions under advisement when considering the cross-border application of those requirements in a future rulemaking.

With respect to AFR and Better Markets' contentions that the Commission should not permit derivatives dealers located within the U.S. to engage in transactions using U.S. personnel on U.S. soil without being subject to U.S. law, the Proposed Rule clearly stated that the Commission recognized that a person that, in connection with its dealing activity, engages in market-facing activity using personnel located in the United States is conducting a substantial aspect of its dealing business in the United States and is subject to U.S. law. But, because the transactions involve two non-U.S. persons, and the financial risk of the transactions lies primarily outside the United States, the Commission also recognized that it must consider the extent to which the underlying regulatory objectives of the Dodd-Frank Act would be advanced in light of other policy considerations, including undue market distortions and international comity, when making a determination of the extent to which the Dodd-Frank Act swap requirements should apply to ANE Transactions.

With respect to AIMA's comment encouraging the CFTC to adopt the SEC's approach with respect to ANE Transactions by requiring counting of ANE Transactions toward the SD registration threshold, the Commission sees little value in requiring counting of ANE Transactions when, if such counting resulted in SD registration, such ANE Transactions would not be subject to most of the SD requirements. ANE Transactions by definition are swaps between non-U.S. persons, the risk of which lies primarily outside of the U.S., and which, in accordance with the Commission's determination above and the regulatory exceptions discussed immediately below, are generally excepted from the group B and C requirements.

VI. Exceptions From Group B and Group C Requirements, Substituted Compliance for Group A and Group B Requirements, and Comparability Determinations

As discussed in the Proposed Rule, Title VII of the Dodd-Frank Act and Commission regulations thereunder establish a broad range of requirements applicable to SDs and MSPs, including requirements regarding risk management and internal and external business conduct.[351] These requirements are designed to reduce systemic risk, increase counterparty protections, and increase market efficiency, orderliness, and transparency.[352] Consistent with the Guidance,[353] SDs and MSPs (whether or not U.S. persons) are subject to all of the Commission regulations described below by virtue of their status as Commission registrants. Put differently, the Commission's view is that if an entity is required to register as an SD or MSP under the Commission's interpretation of section 2(i) of the CEA, then such entity should be subject to these regulations with respect to all of its swap activities. As explained further below, such an approach is necessary because of the important role that the SD and MSP requirements play in the proper operation of a registrant.

However, consistent with section 2(i) of the CEA, in the interest of international comity, and for other reasons discussed in this release, the Commission is providing exceptions from, and a substituted compliance process for, certain regulations applicable to registered SDs and MSPs, as appropriate.[354] Further, the Final

[350] *See* ANE Request for Comment, *supra* note 12.

[351] *See* Proposed Rule, 85 FR at 979–980.

[352] *See, e.g.,* Entities Rule, 77 FR at 30629, 30703.

[353] *See* Guidance, 78 FR at 45342. The Commission notes that while the Guidance states that all swap entities (wherever located) are subject to all of the CFTC's Title VII requirements, the Guidance went on to describe how and when the Commission would expect swap entities to comply with specific requirements and when substituted compliance would be available under its non-binding framework.

[354] As noted in the Proposed Rule, the Commission intends to separately address the cross-border application of Title VII requirements not addressed in the Final Rule (*e.g.,* capital adequacy, clearing and swap processing, mandatory trade execution, swap data repository reporting, large trader reporting, and real-time public reporting)

Continued

Rule creates a framework for comparability determinations that emphasizes a holistic, outcomes-based approach that is grounded in principles of international comity.

A. Classification and Application of Certain Regulatory Requirements—Group A, Group B, and Group C Requirements

As discussed in the Proposed Rule, the Guidance applied a bifurcated approach to the classification of certain regulatory requirements applicable to SDs and MSPs, based on whether the requirement applies to the firm as a whole (''Entity-Level Requirement'' or ''ELR'') or to the individual swap or trading relationship (''Transaction-Level Requirement'' or ''TLR'').[355]

The Guidance categorized the following regulatory requirements as ELRs: (1) Capital adequacy; (2) chief compliance officer (''CCO''); (3) risk management; (4) swap data recordkeeping; (5) swap data repository (''SDR'') reporting; and (6) large trader reporting.[356] The Guidance further divided ELRs into two subcategories.[357] The first category of ELRs includes: (1) Capital adequacy; (2) CCO; (3) risk management; and (4) certain swap data recordkeeping requirements [358] (''First Category ELRs'').[359] The second category of ELRs includes: (1) SDR reporting; (2) certain aspects of swap data recordkeeping relating to complaints and marketing and sales materials under § 23.201(b)(3) and (4); and (3) large trader reporting (''Second Category ELRs'').[360]

The Guidance categorized the following regulatory requirements as TLRs: (1) Required clearing and swap processing; (2) margin (and segregation) for uncleared swaps; (3) mandatory trade execution; (4) swap trading relationship documentation; (5) portfolio reconciliation and compression; (6) real-time public reporting; (7) trade confirmation; (8) daily trading records; and (9) external business conduct standards.[361] As with the ELRs, the Guidance similarly subdivided TLRs into two subcategories.[362] The Commission determined that all TLRs, other than external business conduct standards, address risk mitigation and market transparency.[363] Accordingly, under the Guidance, all TLRs except external business conduct standards are classified as ''Category A TLRs,'' whereas external business conduct standards are classified as ''Category B TLRs.'' [364] Under the Guidance, generally, whether a specific Commission requirement applies to a swap entity and a swap and whether substituted compliance is available depends on the classification of the requirement as an ELR or TLR and the sub-classification of each and the type of swap entity and, in certain cases, the counterparty to a specific swap.[365]

To avoid confusion that may have arisen from using the ELR/TLR classification in the Proposed Rule, given that the Proposed Rule did not address the same set of Commission regulations as the Guidance, the Commission proposed to classify certain of its regulations as group A, group B, and group C requirements for purposes of determining the availability of certain exceptions from, and/or substituted compliance for, such regulations. The Commission requested comment on the group A, group B, and group C requirement classifications and on whether any modifications should be made to the set of requirements in such groups.[366]

The Commission received several comments on its proposed use of the group A, group B, and group C requirements classifications. IIB/SIFMA and JFMC/IBAJ generally supported the Proposed Rule's classification of swap entity requirements. However, IIB/SIFMA requested that the Commission expand and clarify such categorization in certain respects (discussed in the relevant sections below) to align the cross-border application of the Commission's requirements with the policy objectives for those requirements. AIMA stated its belief that any swap involving a non-U.S. person (even where its counterparty is a U.S. person) should also be able to use substituted compliance and encouraged the CFTC to review the group B and group C requirements with this approach in mind, but did not provide any specific recommended changes to those classifications. IATP stated that it was not clear which set of regulations were covered by the Proposed Rule that are not covered by the Guidance and that, without a comparative summary of the different set of regulations covered by each, there is no grounds to judge readily why the Commission proposed to abandon the readily understood ''entity level'' and ''transaction level'' requirement classifications to compare for granting substituted compliance to foreign regulatory regimes.

After considering the comments, the Commission continues to believe that classifying certain of its regulations as group A, group B, and group C requirements is appropriate and helpful for purposes of determining the availability of certain exceptions from, and/or substituted compliance for, such regulations.[367] The proposed and final group A, group B, and group C requirements are discussed below.

1. Group A Requirements

(i) Proposed Rule

The Commission proposed that the group A requirements would include: (1) CCO; (2) risk management; (3) swap data recordkeeping; and (4) antitrust considerations. Specifically, under the Proposed Rule, the group A requirements consisted of the requirements set forth in §§ 3.3, 23.201, 23.203, 23.600, 23.601, 23.602, 23.603, 23.605, 23.606, 23.607, and 23.609.[368] As discussed in the Proposed Rule, the Commission believes that the group A requirements would be impractical to apply only to specific transactions or counterparty relationships and are most effective when applied consistently across the entire enterprise, noting that they ensure that swap entities implement and maintain a comprehensive and robust system of internal controls to ensure the financial integrity of the firm, and, in turn, the protection of the financial system. Further, the Commission noted that, together with other Commission requirements, the proposed group A requirements constitute an important line of defense against financial, operational, and compliance risks that could lead to a firm's default; and, further, that requiring swap entities to rigorously monitor and address the risks they incur as part of their day-to-day businesses lowers the registrants' risk of default—and ultimately protects the public and the financial system. For this reason, the Commission stated that it

(hereinafter, the ''Unaddressed Requirements''). In that regard, the Commission notes that it adopted capital adequacy and related financial reporting requirements for SDs and MSPs at its open meeting on July 22, 2020.

[355] *See, e.g.,* Guidance, 78 FR at 45331.

[356] *See, e.g., id.*

[357] *See, e.g., id.*

[358] Swap data recordkeeping under 17 CFR 23.201 and 23.203 (except certain aspects of swap data recordkeeping relating to complaints and sales materials).

[359] *See, e.g.,* Guidance, 78 FR at 45331.

[360] *See, e.g., id.*

[361] *See, e.g., id.* at 45333.

[362] *See, e.g., id.*

[363] *See, e.g., id.*

[364] *See, e.g., id.*

[365] *See, e.g., id.* at 45337–45338.

[366] Proposed Rule, 85 FR at 982.

[367] With respect to AIMA's comment, the Commission notes that the Proposed Rule provided a summary of all of the requirements addressed by the Guidance and which requirements were addressed in the Proposed Rule.

[368] 17 CFR 3.3, 23.201, 23.203, 23.600, 23.601, 23.602, 23.603, 23.605, 23.606, 23.607, and 23.609.

has strong supervisory interests in ensuring that swap entities (whether domestic or foreign) are subject to the group A requirements or comparably rigorous standards.[369]

Each of the proposed group A requirements is discussed in more detail below.

(a) Chief Compliance Officer

Section 4s(k) of the CEA requires that each SD and MSP designate an individual to serve as its CCO and specifies certain duties of the CCO.[370] Pursuant to section 4s(k), the Commission adopted § 3.3,[371] which requires SDs and MSPs to designate a CCO responsible for administering the firm's compliance policies and procedures, reporting directly to the board of directors or a senior officer of the SD or MSP, as well as preparing and filing with the Commission a certified annual report discussing the registrant's compliance policies and activities. The CCO function is an integral element of a firm's risk management and oversight, as well as the Commission's effort to foster a strong culture of compliance within SDs and MSPs.

(b) Risk Management

Section 4s(j) of the CEA requires each SD and MSP to establish internal policies and procedures designed to, among other things, address risk management, monitor compliance with position limits, prevent conflicts of interest, and promote diligent supervision, as well as maintain business continuity and disaster recovery programs.[372] The Commission implemented these provisions in §§ 23.600, 23.601, 23.602, 23.603, 23.605, and 23.606.[373] The Commission also adopted § 23.609,[374] which requires certain risk management procedures for SDs or MSPs that are clearing members of a DCO.[375] Collectively, these requirements help to establish a comprehensive internal risk management program for SDs and MSPs, which is critical to effective systemic risk management for the overall swap market.

(c) Swap Data Recordkeeping

CEA section 4s(f)(1)(B) requires SDs and MSPs to keep books and records for all activities related to their swap business.[376] Sections 4s(g)(1) and (4) require SDs and MSPs to maintain trading records for each swap and all related records, as well as a complete audit trail for comprehensive trade reconstructions.[377] Additionally, CEA section 4s(f)(1) requires SDs and MSPs to ''make such reports as are required by the Commission by rule or regulation regarding the transactions and positions and financial condition of'' the registered SD or MSP.[378] Further, CEA section 4s(h) requires SDs and MSPs to ''conform with such business conduct standards . . . as may be prescribed by the Commission by rule or regulation.''[379]

Pursuant to these provisions, the Commission promulgated final rules that set forth certain reporting and recordkeeping requirements for SDs and MSPs.[380] Specifically, §§ 23.201 and 23.203[381] require SDs and MSPs to keep records including complete transaction and position information for all swap activities (*e.g.,* documentation on which trade information is originally recorded). In particular, § 23.201 states that each SD and MSP shall keep full, complete, and systematic records of all activities related to its business as a SD or MSP.[382] Such records must include, among other things, a record of each complaint received by the SD or MSP concerning any partner, member, officer, employee, or agent,[383] as well as all marketing and sales presentations, advertisements, literature, and communications.[384] Commission regulation 23.203[385] requires, among other things, that records (other than swap data reported in accordance with part 45 of the Commission's regulations[386]) be maintained in accordance with § 1.31.[387] Commission regulation 1.31 requires that records relating to swaps be maintained for specific durations, including that records of swaps be maintained for a minimum of five years and as much as the life of the swap plus five years, and that most records be ''readily accessible'' for the entire recordkeeping period.[388]

(d) Antitrust Considerations

Section 4s(j)(6) of the CEA prohibits an SD or MSP from adopting any process or taking any action that results in any unreasonable restraint of trade or imposes any material anticompetitive burden on trading or clearing, unless necessary or appropriate to achieve the purposes of the CEA.[389] The Commission promulgated this requirement in § 23.607(a)[390] and also adopted § 23.607(b), which requires SDs and MSPs to adopt policies and procedures to prevent actions that result in unreasonable restraints of trade or impose any material anticompetitive burden on trading or clearing.[391]

(ii) Summary of Comments

JFMC/IBAJ and IIB/SIFMA were supportive of the streamlining of the Commission's recordkeeping requirements under § 23.201 as group A requirements (which the Guidance separated into two different subcategories). JFMC/IBAJ also requested the Commission explicitly categorize § 1.31 as a group A requirement in furtherance of the goal of providing legal certainty and streamlining recordkeeping requirements. IIB/SIFMA requested that the Commission include §§ 1.31 and 45.2 as group A requirements, which they stated would be consistent with categorizing § 23.203 as a group A requirement. IIB/SIFMA also was supportive of including the Commission's antitrust rules (which were not addressed by the Guidance) as a group A requirement.

(iii) Final Rule

After carefully considering the comments, the Commission is adopting the proposed group A requirements and adding § 45.2(a) to the group A requirements to the extent it duplicates § 23.201, as shown in the rule text in

[369] *See* Proposed Rule, 85 FR at 980–981.

[370] 7 U.S.C. 6s(k).

[371] 17 CFR 3.3. *See* Swap Dealer and Major Swap Participant Recordkeeping, Reporting, and Duties Rules; Futures Commission Merchant and Introducing Broker Conflicts of Interest Rules; Chief Compliance Officer Rules for Swap Dealers, Major Swap Participants, and Futures Commission Merchants, 77 FR 20128 (Apr. 3, 2012) (''Final SD and MSP Recordkeeping, Reporting, and Duties Rule''). In 2018, the Commission adopted amendments to the CCO requirements. *See* Chief Compliance Officer Duties and Annual Report Requirements for Futures Commission Merchants, Swap Dealers, and Major Swap Participants, 83 FR 43510 (Aug. 27, 2018).

[372] 7 U.S.C. 6s(j).

[373] 17 CFR 23.600, 23.601, 23.602, 23.603, 23.605, and 23.606. *See* Final SD and MSP Recordkeeping, Reporting, and Duties Rule, 77 FR 20128 (addressing rules related to risk management programs, monitoring of position limits, diligent supervision, business continuity and disaster recovery, conflicts of interest policies and procedures, and general information availability).

[374] 17 CFR 23.609.

[375] *See* Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management, 77 FR 21278 (Apr. 9, 2012).

[376] 7 U.S.C. 6s(f)(1)(B).

[377] 7 U.S.C. 6s(g)(1) and (4).

[378] 7 U.S.C. 6s(f)(1).

[379] 7 U.S.C. 6s(h)(1). *See* 7 U.S.C. 6s(h)(3).

[380] *See* Final SD and MSP Recordkeeping, Reporting, and Duties Rule, 77 FR 20128.

[381] 17 CFR 23.201 and 203.

[382] 17 CFR 23.201(b).

[383] 17 CFR 23.201(b)(3)(i).

[384] 17 CFR 23.201(b)(4).

[385] 17 CFR 23.203.

[386] 17 CFR 45.

[387] 17 CFR 1.31.

[388] 17 CFR 1.31(b).

[389] 7 U.S.C. 6s(j)(6).

[390] 17 CFR 23.607(a).

[391] 17 CFR 23.607(b).

this release.[392] The Commission is making this addition to clarify that, to the extent the same substantive recordkeeping requirement is included in both §§ 23.201 and 45.2(a),[393] each is a group A requirement for which substituted compliance may be available, as discussed in section VI.C below.[394]

Regarding the comments to include § 1.31 as a group A requirement, § 1.31 is a general requirement providing maintenance and access requirements for many regulatory records, and not only those required under the group A requirements. Further, to the extent an SD/MSP receives substituted compliance for a group A requirement, such as § 23.203, that incorporates § 1.31's recordkeeping requirements for certain regulatory records, the Commission's view is that § 1.31 would also not apply to such regulatory records. Therefore, the Commission is declining to include § 1.31 as a group A requirement.

2. Group B Requirements

(i) Proposed Rule

The Commission proposed that the group B requirements would include: (1) Swap trading relationship documentation; (2) portfolio reconciliation and compression; (3) trade confirmation; and (4) daily trading records. Specifically, under the Proposed Rule, the group B requirements consist of the requirements set forth in §§ 23.202, 23.501, 23.502, 23.503, and 23.504.[395] As discussed in the Proposed Rule, the group B requirements relate to risk mitigation and the maintenance of good recordkeeping and business practices.[396] The Commission stated that, unlike for the group A requirements, it believes that the group B requirements can practically be applied on a bifurcated basis between domestic and foreign transactions or counterparty relationships and, thus, do not need to be applied uniformly across an entire enterprise. Therefore, the Commission stated that it can have greater flexibility with respect to the application of these requirements to non-U.S. swap entities and foreign branches of U.S. swap entities.[397]

Each of the proposed group B requirements is discussed in more detail below.

(a) Swap Trading Relationship Documentation

CEA section 4s(i) requires each SD and MSP to conform to Commission standards for the timely and accurate confirmation, processing, netting, documentation, and valuation of swaps.[398] Pursuant to section 4s(i), the Commission adopted, among other regulations, § 23.504.[399] Regulation 23.504(a) requires SDs and MSPs to ''establish, maintain and follow written policies and procedures'' to ensure that the SD or MSP executes written swap trading relationship documentation, and § 23.504(c) requires that documentation policies and procedures be audited periodically by an independent auditor to identify material weaknesses.[400] Under § 23.504(b), the swap trading relationship documentation must include, among other things: (1) All terms governing the trading relationship between the SD or MSP and its counterparty; (2) credit support arrangements; (3) investment and re-hypothecation terms for assets used as margin for uncleared swaps; and (4) custodial arrangements.[401] Swap documentation standards facilitate sound risk management and may promote standardization of documents and transactions, which are key conditions for central clearing, and lead to other operational efficiencies, including improved valuation.

(b) Portfolio Reconciliation and Compression

CEA section 4s(i) directs the Commission to prescribe regulations for the timely and accurate processing and netting of all swaps entered into by SDs and MSPs.[402] Pursuant to CEA section 4s(i), the Commission adopted §§ 23.502 and 23.503,[403] which require SDs and MSPs to perform portfolio reconciliation and compression for their swaps.[404] Portfolio reconciliation is a post-execution risk management tool designed to ensure accurate confirmation of a swap's terms and to identify and resolve any discrepancies between counterparties regarding the valuation of the swap. Portfolio compression is a post-trade processing and netting mechanism that is intended to ensure timely, accurate processing and netting of swaps.[405] Further, § 23.503 requires all SDs and MSPs to establish policies and procedures for terminating fully offsetting uncleared swaps, when appropriate, and periodically participating in bilateral and/or multilateral portfolio compression exercises for uncleared swaps with other SDs or MSPs or through a third party.[406] The rule also requires policies and procedures for engaging in such exercises for uncleared swaps with non-SDs and non-MSPs upon request.[407]

(c) Trade Confirmation

Section 4s(i) of the CEA requires that each SD and MSP must comply with the Commission's regulations prescribing timely and accurate confirmation of swaps.[408] The Commission adopted § 23.501,[409] which requires, among other things, timely and accurate confirmation of swap transactions (which includes execution, termination, assignment, novation, exchange, transfer, amendment, conveyance, or extinguishing of rights or obligations of a swap) among SDs and MSPs by the end of the first business day following the day of execution.[410] Timely and accurate confirmation of swaps—together with portfolio reconciliation and compression—is an important post-

[392] Final § 23.23(a)(6).

[393] Commission regulation 23.201 requires, in relevant part, that each SD and MSP keep full, complete, and systematic records, together with all pertinent data and memoranda, of all its swaps activities and its activities related to its business as a SD or MSP. Commission regulation 45.2(a) requires, in relevant part, that each SD and MSP subject to the jurisdiction of the Commission shall keep full, complete, and systematic records, together with all pertinent data and memoranda, of all activities relating to the business of such entity or person with respect to swaps, as prescribed by the Commission.

[394] Similarly, the Commission will view any previously issued comparability determination that allows substituted compliance for § 23.201 to also allow for substituted compliance with § 45.2(a) to the extent it duplicates § 23.201.

[395] 17 CFR 23.202, 23.501, 23.502, 23.503, and 23.504.

[396] *See, e.g.,* Int'l Org. of Sec. Comm'ns, Risk Mitigation Standards for Non-Centrally Cleared OTC Derivatives, IOSCO Doc. FR01/2015 (Jan. 28, 2015) (''IOSCO Risk Management Standards''), available at *https://www.iosco.org/library/pubdocs/pdf/IOSCOPD469.pdf* (discussing, among other things, the objectives and benefits of trading relationship documentation, trade confirmation, reconciliation, and portfolio compression requirements). In addition, the group B requirements also provide customer protection and market transparency benefits.

[397] *See* Proposed Rule, 85 FR at 981–982.

[398] 7 U.S.C. 6s(i).

[399] 17 CFR 23.504. *See* Confirmation, Portfolio Reconciliation, Portfolio Compression, and Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants, 77 FR 55904 (Sept. 11, 2012) (''Final Confirmation, Risk Mitigation, and Documentation Rules'').

[400] 17 CFR 23.504(a)(2) and (c).

[401] 17 CFR 23.504(b).

[402] 7 U.S.C. 6s(i).

[403] 17 CFR 23.502 and 503. *See* Final Confirmation, Risk Mitigation, and Documentation Rules, 77 FR 55904.

[404] *See* 17 CFR 23.502 and 503.

[405] For example, the reduced transaction count may decrease operational risk as there are fewer trades to maintain, process, and settle.

[406] *See* 17 CFR 23.503(a).

[407] 17 CFR 23.503(b).

[408] 7 U.S.C. 6s(i).

[409] 17 CFR 23.501. *See* Final Confirmation, Risk Mitigation, and Documentation Rules, 77 FR 55904.

[410] 17 CFR 23.501(a)(1).

trade processing mechanism for reducing risks and improving operational efficiency.[411]

(d) Daily Trading Records

Pursuant to CEA section 4s(g),[412] the Commission adopted § 23.202,[413] which requires SDs and MSPs to maintain daily trading records, including records of trade information related to pre-execution, execution, and post-execution data that is needed to conduct a comprehensive and accurate trade reconstruction for each swap. The regulation also requires that records be kept of cash or forward transactions used to hedge, mitigate the risk of, or offset any swap held by the SD or MSP.[414] Accurate and timely records regarding all phases of a swap transaction can serve to greatly enhance a firm's internal supervision, as well as the Commission's ability to detect and address market or regulatory abuses or evasion.

(ii) Summary of Comments

IIB/SIFMA stated that they support the Commission's proposed categorization of the group B requirements, but requested that the Commission recategorize its pre-execution daily trading records requirements under § 23.202 as group C requirements instead of group B requirements. IIB/SIFMA asserted that pre-execution information generally has no nexus to the risk management of the swap entity or to the Commission's risk mitigation rules and instead relate to a swap entity's sales practices.

(iii) Final Rule

After carefully considering the comments, the Commission is adopting the group B requirements as proposed.[415] With respect to the request to make pre-execution trading records requirements a group C requirement, accurate and timely records regarding all phases of a swap transaction (including pre-execution trading records) can serve to greatly enhance a firm's internal supervision, as well as the Commission's ability to detect and address market or regulatory abuses or evasion. Because these records relate to market integrity (and not only customer protection), the Commission believes the pre-execution trading records requirements should continue to be group B requirements and not be eligible for the exceptions the Final Rule provides from the group C requirements.

3. Group C Requirements

(i) Proposed Rule

Pursuant to CEA section 4s(h),[416] the Commission adopted external business conduct rules, which establish certain additional business conduct standards governing the conduct of SDs and MSPs in dealing with their swap counterparties.[417] The Commission proposed that the group C requirements would consist of these rules, which are set forth in §§ 23.400 through 23.451.[418] As discussed in the Proposed Rule, broadly speaking, these rules are designed to enhance counterparty protections by establishing robust requirements regarding SDs' and MSPs' conduct with their counterparties. Under these rules, SDs and MSPs are required to, among other things, conduct due diligence on their counterparties to verify eligibility to trade (including eligible contract participant (''ECP'') status), refrain from engaging in abusive market practices, provide disclosure of material information about the swap to their counterparties, provide a daily mid-market mark for uncleared swaps, and, when recommending a swap to a counterparty, make a determination as to the suitability of the swap for the counterparty based on reasonable diligence concerning the counterparty.

As the Commission discussed in the Proposed Rule, the group C requirements have a more attenuated link to, and are therefore distinguishable from, systemic and market-oriented protections in the group A and group B requirements. Additionally, the Commission noted its belief that the foreign jurisdictions in which non-U.S. persons and foreign branches of U.S. swap entities are located are likely to have a significant interest in the type of business conduct standards that would be applicable to transactions with such non-U.S. persons and foreign branches within their jurisdiction, and, consistent with section 2(i) of the CEA and in the interest of international comity, it is generally appropriate to defer to such jurisdictions in applying, or not applying, such standards to foreign-based swaps with foreign counterparties.[419]

(ii) Summary of Comments

IIB/SIFMA supported the Proposed Rule's categorization of the Commission's external business conduct standards as group C requirements because the approach is consistent with the Guidance, and these requirements focus on counterparty protection. However, IIB/SIFMA requested that the Commission add its rules for elective initial margin segregation to the list of group C requirements.[420] They argued that these rules found in part 23, subpart L (§§ 23.700–23.704) (''Subpart L''),[421] like the proposed group C requirements, are largely focused on customer protection rather than risk mitigation.

(iii) Final Rule

After careful consideration of the comments, the Commission is adopting the group C requirements as proposed and adding the requirements of Subpart L as group C requirements, as shown in the rule text in this release.[422]

Section 724(c) of the Dodd-Frank Act amended the CEA to add section 4s(l),[423] which addresses segregation of initial margin held as collateral in uncleared swap transactions (*i.e.,* swaps not submitted for clearing on a DCO). Section 4s(l) was implemented in Subpart L, which imposes requirements on SDs and MSPs with respect to the treatment of collateral posted by their counterparties to margin, guarantee, or secure certain uncleared swaps.[424] Specifically, § 23.701 requires, except in those circumstances where segregation is mandatory under the Margin Rules,

[411] Additionally, the Commission notes that § 23.504(b)(2) requires that the swap trading relationship documentation of SDs and MSPs must include all confirmations of swap transactions. 17 CFR 23.504(b)(2).

[412] 7 U.S.C. 6s(g).

[413] 17 CFR 23.202. *See* Final SD and MSP Recordkeeping, Reporting, and Duties Rule, 77 FR 20128.

[414] 17 CFR 23.202(b).

[415] Final § 23.23(a)(7).

[416] 7 U.S.C. 6s(h).

[417] *See* Business Conduct Standards for Swap Dealers and Major Swap Participants with Counterparties, 77 FR 9734 (Feb. 17, 2012).

[418] 17 CFR 23.400–23.451.

[419] *See* Proposed Rule, 85 FR at 982.

[420] As noted in the discussion of the group B requirements, IIB/SIFMA also requested that the Commission recategorize pre-execution daily trading records rules as group C requirements (not group B requirements).

[421] 17 CFR part 23, subpart L.

[422] Final § 23.23(a)(8).

[423] 7 U.S.C. 6s(l).

[424] Protection of Collateral of Counterparties to Uncleared Swaps; Treatment of Securities in a Portfolio Margining Account in a Commodity Broker Bankruptcy, 78 FR 66621 (Nov. 2013). The Commission later amended Subpart L in light of the Commission's adoption of subpart E of part 23 (Capital and Margin Requirements for Swap Dealers and Major Swap Participants) in January 2016 and the prudential regulators' adoption of similar rules in November 2015 (together, ''Margin Rules''), which, among other things, established initial margin requirements applicable to SDs and MSPs. As a result, Subpart L's segregation requirements apply only when the Margin Rules' segregation requirements do not. Further, the Commission understands that counterparties have elected segregation under Subpart L very rarely. *See, e.g.,* Segregation of Assets Held as Collateral in Uncleared Swap Transactions, 84 FR 12894 (Apr. 2019).

that a SD/MSP provide notice to its counterparty of its right to have Initial Margin (''IM'') [425] provided by it to the SD/MSP segregated in accordance with §§ 23.702 and 23.703.[426] Commission regulations 23.702 and 23.703 provide requirements for segregation and investment of IM where the counterparty elects such segregation,[427] and § 23.704 requires that each SD/MSP report quarterly to each counterparty that does not choose to require IM segregation that the back office procedures of the SD/MSP relating to margin and collateral requirements are in compliance with the agreement of the counterparties.[428]

The Commission agrees with IIB/SIFMA that these requirements are focused on customer protection rather than risk mitigation and are appropriately included as group C requirements. In this regard, the Commission notes, specifically, that Subpart L leaves to the discretion of the counterparty to the SD/MSP whether IM is segregated, rather than mandating its segregation, and has largely been superseded by the Margin Rules, which specifically address systemic risk in relation to margin for uncleared swaps.

B. Exceptions From Group B and Group C Requirements

1. Proposed Exceptions, Generally

(i) Proposed Rule

Consistent with section 2(i) of the CEA, the Commission proposed four exceptions from certain Commission regulations for foreign-based swaps in the Proposed Rule.[429]

First, the Commission proposed an exception from certain group B and C requirements for certain anonymous, exchange-traded, and cleared foreign-based swaps (''Exchange-Traded Exception'').

Second, the Commission proposed an exception from the group C requirements for certain foreign-based swaps with foreign counterparties (''Foreign Swap Group C Exception'').

Third, the Commission proposed an exception from the group B requirements for certain foreign-based swaps of foreign branches of U.S. swap entities with certain foreign counterparties, subject to certain limitations, including a quarterly cap on the amount of such swaps (''Limited Foreign Branch Group B Exception'').[430]

Fourth, the Commission proposed an exception from the group B requirements for the foreign-based swaps of certain non-U.S. swap entities with certain foreign counterparties (''Non-U.S. Swap Entity Group B Exception'').

While these exceptions each have different eligibility requirements, a common requirement is that they would be available only to foreign-based swaps,[431] as other swaps would be treated as domestic swaps for purposes of applying the group B and group C requirements and, therefore, would not be eligible for the above exceptions. Further, swap entities that avail themselves of these exceptions for their foreign-based swaps would be required to comply with the applicable laws of the foreign jurisdiction(s) to which they are subject, rather than the relevant Commission requirements, for such swaps; however, notwithstanding these exceptions, swap entities would remain subject to the CEA and Commission regulations not covered by the exceptions, including the prohibition on the employment, or attempted employment, of manipulative and deceptive devices in § 180.1.[432] The Commission also would expect swap entities to address any significant risk that may arise as a result of the utilization of one or more exceptions in their risk management programs required pursuant to § 23.600.[433]

The Commission requested comments on whether, in light of the Commission's supervisory interests, the proposed exceptions were appropriate or whether they should be broadened or narrowed.[434]

(ii) Summary of Comments

JFMC/IBAJ generally supported the proposed exceptions to the application of group B and C requirements under the Proposed Rule, stating that they believe the exceptions generally strike the right balance in protecting the integrity, safety, and soundness of the U.S. financial system while recognizing the principles of international comity. ISDA stated that it supported the Commission's intent to place non-U.S. swap entities (that are Other Non-U.S. Persons) and foreign branches of U.S. swap entities on equal footing with respect to the cross-border application of certain CFTC requirements, noting that foreign branches of U.S. swap entities are subject to the laws of the foreign jurisdictions in which they operate and, thus, imposing U.S. requirements on these entities results in duplicative regulation—increasing compliance costs, complexity, and inefficiencies. However, JFMC/IBAJ, ISDA, and IIB/SIFMA requested that the Commission expand and clarify the Proposed Rule's exceptions in certain specific respects, which are discussed in the relevant sections below. AFR asserted that the Proposed Rule would allow branches of U.S. persons, which are actually formally and legally part of the parent U.S. organization, to effectively act as non-U.S. persons.[435] IATP stated that it only understands the Exchange-Traded Exception and did not comment on the other proposed exceptions. Its comment on the proposed Exchange-Traded Exception is discussed below.

2. Exchange-Traded Exception

(i) Proposed Rule

The Commission proposed that, with respect to its foreign-based swaps, each non-U.S. swap entity and foreign branch of a U.S. swap entity would be excepted from the group B requirements (other than the daily trading records requirements in §§ 23.202(a) through 23.202(a)(1) [436]) and the group C requirements with respect to any swap entered into on a DCM, a registered SEF or a SEF exempted from registration by the Commission pursuant to section 5h(g) of the CEA, or an FBOT registered with the Commission pursuant to part 48 of its regulations [437] where, in each case, the swap is cleared through a registered DCO or a clearing organization that has been exempted from registration by the Commission

[425] ''Initial Margin'' is defined in § 23.700 for purposes of Subpart L as money, securities, or property posted by a party to a swap as performance bond to cover potential future exposures arising from changes in the market value of the position. 17 CFR 23.700.

[426] 17 CFR 23.701.

[427] 17 CFR 23.702 and 703.

[428] 17 CFR 23.704.

[429] *See* Proposed Rule, 85 FR at 982–984.

[430] This exception was defined as the ''Foreign Branch Group B Exception'' in the Proposed Rule. The Commission is adding the word ''Limited'' to the beginning of the defined term, to reflect the conditions that apply to the use of the exception, including the cap on its use in a calendar quarter.

[431] As discussed in section II.I, *supra,* a foreign-based swap means: (1) A swap by a non-U.S. swap entity, except for a swap booked in a U.S. branch; or (2) A swap conducted through a foreign branch.

[432] 17 CFR 180.1.

[433] 17 CFR 23.600.

[434] Proposed Rule, 85 FR at 984.

[435] The Commission disagrees with this assertion. For example, under the Proposed Rule, group B requirements apply more broadly to foreign branches than to non-U.S. persons due to the limited scope of the Limited Foreign Branch Group B Exception as compared to the Non-U.S. Swap Entity Group B Exception (each discussed below), and foreign branches (as a part of a U.S. person) are not eligible for substituted compliance for the group A requirements.

[436] 17 CFR 23.202(a) through (a)(1).

[437] The Commission stated that it would consider the proposed exception also to apply with respect to an FBOT that provides direct access to its order entry and trade matching system from within the U.S. pursuant to no-action relief issued by Commission staff.

pursuant to section 5b(h) of the CEA, and the swap entity does not know the identity of the counterparty to the swap prior to execution.[438]

With respect to the group B trade confirmation requirement, the Commission noted that where a cleared swap is executed anonymously on a DCM or SEF (as discussed above), independent requirements that apply to DCM and SEF transactions pursuant to the Commission's regulations should ensure that these requirements are met.[439] And, for a combination of reasons, including the fact that a registered FBOT is analogous to a DCM and is expected to be subject to comprehensive supervision and regulation in its home country,[440] and the fact that the swap will be cleared, the Commission believes that the Commission's trade confirmation requirements should not apply to foreign-based swaps that meet the requirements of the exception and are traded on registered FBOTs.

Of the remaining group B requirements, the Commission noted that the portfolio reconciliation and compression and swap trading relationship documentation requirements would not apply to the cleared DCM, SEF, or FBOT transactions described above because the Commission regulations that establish those requirements make clear that they do not apply to cleared transactions.[441] For the last group B requirement—the daily trading records requirement[442]—the Commission stated that it believes that, as a matter of international comity and recognizing the supervisory interests of foreign regulators who may have their own trading records requirements, it is appropriate to except such foreign-based swaps from certain of the Commission's daily trading records requirements. However, the Commission stated that the requirements of § 23.202(a) through (a)(1) should continue to apply, as all swap entities should be required to maintain, among other things, sufficient records to conduct a comprehensive and accurate trade reconstruction for each swap. The Commission noted that, in particular, for certain pre-execution trade information under § 23.202(a)(1),[443] the swap entity may be the best, or only, source for such records, and for this reason, paragraphs (a) through (a)(1) of § 23.202 are carved out from the group B requirements in the proposed exception.

Additionally, the Commission noted that, given that this exception is predicated on anonymity, many of the group C requirements would be inapplicable.[444] Further, because the Commission believes a registered FBOT is analogous to a DCM for these purposes and is expected to be subject to comprehensive supervision and regulation in its home country, and because a SEF that is exempted from registration by the Commission pursuant to section 5h(g) of the CEA must be subject to supervision and regulation that is comparable to that to which Commission-registered SEFs are subject, the Commission also proposed that these group C requirements would not be applicable where such a swap is executed anonymously on a registered FBOT, or a SEF that has been exempted from registration with the Commission pursuant to section 5h(g) of the CEA, and cleared. In the interest of international comity and because the proposed exception requires that the swap be exchange-traded and cleared, the Commission proposed that foreign-based swaps would also be excepted from the remaining group C requirements in these circumstances. The Commission noted that it expects that the requirements that the swaps be exchange-traded and cleared will generally limit swaps that benefit from the exception to standardized and commonly-traded, foreign-based swaps, for which the Commission believes application of the remaining group C requirements is not necessary.

(ii) Summary of Comments

IIB/SIFMA requested that the Commission expand the exception to apply to all anonymous cleared swaps (whether or not the trading venue and clearing organization are registered or exempt from registration with the Commission), in light of the risk mitigating effects of central clearing and the regulatory compliance and market integrity protections of trading anonymously on a regulated platform. They stated that it is not necessary for the Commission to limit this exception for anonymous cleared swaps in a manner that would indirectly expand the SEF and DCO registration requirements to non-U.S. trading venues and clearing organizations with non-U.S. swap entity participants. Further, they asserted that if the counterparty to a swap was a U.S. person, the Commission's SEF and DCO registration requirements would independently require the trading venue and clearing organization to register with the Commission or obtain an exemption from registration. Additionally, IIB/SIFMA requested the exception be made available to U.S. swap entities, as well, except for daily trading records rules, arguing that the interposition of clearing organizations reduces risk to the United States, thereby obviating the need to apply the risk mitigation rules (where applicable). They also noted that SEFs provide market participants with the regulatory compliance protections associated with centralized trading and that many group C requirements already do not apply to a swap entity in connection with swaps executed anonymously, regardless of the U.S. person status of the swap entity.[445]

ISDA was supportive of the proposed exception, but requested that it be extended to cover: (1) All relevant group B and C requirements; and (2) U.S. and non-U.S. entities' transactions that are SEF- (or exempt SEF-) executed and cleared at a DCO, exempt DCO, or clearinghouse subject to CFTC no-action relief, regardless of whether they are anonymously executed. ISDA noted that one of the regulatory benefits of SEF trading is that market participants receive the necessary regulatory compliance protections associated with centralized trading, and that, as self-regulatory organizations, SEFs (and exempt SEFs) are expected to keep daily trading records and audit trails of each transaction executed on their platforms, so it makes sense to allow counterparties not to comply with group B requirements when executing trades on SEFs (or exempt SEFs), and restricting this exemption to a particular method of execution on a SEF does not serve any regulatory purpose. Moreover, ISDA argued that imposing CFTC external business conduct standards to centrally-executed and cleared trades also creates redundancies, as counterparties that trade on SEFs (or exempt SEFs) receive necessary disclosures as part of the onboarding process and regulatory required pre-trade credit checks ensure that counterparties have sufficient credit to execute transactions.

IATP stated that the biggest exception, in terms of the notional amount of swaps and the number of group B and C requirements that would be exempted

[438] *See* Proposed Rule, 85 FR at 982–983. This approach is similar to the Guidance. *See* Guidance, 78 FR at 45351–45352 and 45360–45361.

[439] *See* 17 CFR 23.501(a)(4)(i) and 37.6(b).

[440] *See* 17 CFR 48.5(d)(2).

[441] *See* 17 CFR 23.502(d), 23.503(c), 23.504(a)(1)(iii).

[442] *See* 17 CFR 23.202.

[443] *See* 17 CFR 23.202(a)(1).

[444] *See* 17 CFR 23.402(b)–(c), 23.430(e), 23.431(c), 23.450(h), 23.451(b)(2)(iii).

[445] In addition to noting the exceptions in the regulations themselves, IIB/SIFMA reference the relief provided by Staff Letter 13–70 for intended to be cleared swaps (''Staff ITBC Letter'').

from compliance, is the Exchange-Traded Exception, and that this exception would comport generally with G20 reform objectives to centrally clear swaps and trade them anonymously (preferably post-trade as well as pre-trade) on regulated exchanges. However, IATP objected to the granting of the exception for foreign SEFs and clearing organizations that have not qualified for registration with the Commission, but have been granted exemptions from registration, presumably in the interest of international comity, noting that if the Exchange-Traded Exception results in disapplication of Commission requirements to customized foreign affiliate swaps traded and cleared on exempted entities, the risks to U.S. ultimate parents could be most unexpected.

(iii) Final Rule

After carefully considering the comments, the Commission is adopting the exception as proposed.[446]

Regarding requests to expand the exception to include all anonymous foreign-based swaps entered into on an exchange and which are subsequently cleared, regardless of whether the exchange and clearing organization are registered or exempt from registration with the Commission, or to include swaps that are cleared on a DCO that has received staff no-action relief from registration requirements, the Commission is declining to expand the exception. As noted in the Proposed Rule, the exception is based, in part, on the swaps eligible for it being subject to independent requirements that apply to transactions on a DCM or registered SEF pursuant to Commission regulations or, with respect to exempt SEFs and registered FBOTs, to comprehensive supervision and regulation in their home countries. Similarly, the Commission believes that limiting the exception to DCOs that are registered or exempt provides assurance that the DCOs clearing swaps eligible for the exception will be subject to comprehensive supervision and regulation. Further, as explained above, the Commission does not find persuasive IIB/SIFMA's argument that if the counterparty to a foreign-based swap is a U.S. person, other Commission rules require that the trade be executed on a registered or exempt SEF and cleared through a registered or exempt DCO.[447] The Commission will consider expanding the exception pending other amendments to the SEF/DCO regulations.

Regarding the request not to require that eligible foreign-based swaps be anonymous, the Commission declines to expand the exception in this manner. The other exceptions in the Final Rule provide relief where appropriate for foreign-based swaps where the counterparty is known, and this limited exception, as in the Guidance, is only meant to provide relief from certain of the group B and group C requirements where the counterparty is unknown and, thus, it would be impractical to comply with such requirements.

Regarding the request to allow U.S. swap entities (other than their foreign branches) to utilize the exception, the Commission declines to expand the exception in this manner. The Commission is of the view, consistent with the Guidance, that where a U.S. swap entity (other than its foreign branch) enters into a swap, that swap is part of the U.S. swap market. And, accordingly, the group B and group C requirements should generally apply fully to such swap entity.[448] In addition, the Commission is generally of the view that the Final Rule is not the appropriate place to make changes to the regulation of the U.S. swap market. Expanding the exception to cover swaps in the U.S. swaps market would require amendments to the underlying group B and group C requirements that apply to all covered swaps rather than creating a limited exception to them for certain foreign swaps. However, as comments were supportive of extending the exception to U.S. swap entities, the Commission will continue to analyze this issue and take these comments into consideration when next considering changes to the group B and group C requirements.

With respect to the request to include pre-execution trading records (*i.e.,* by revising the exception to apply to all group B requirements), the Commission declines to expand the exception in this manner. Excluding pre-execution trading records requirements is consistent with the Guidance and, as noted in the Proposed Rule, these requirements should continue to apply, as all swap entities should be required to maintain, among other things, sufficient records to conduct a comprehensive and accurate trade reconstruction for each swap, and the swap entity may be the best, or only, source for pre-execution trading records.

3. Foreign Swap Group C Exception

(i) Proposed Rule

The Commission proposed that each non-U.S. swap entity and foreign branch of a U.S. swap entity would be excepted from the group C requirements with respect to its foreign-based swaps with a foreign counterparty.[449] The Commission noted that such swaps would not include as a party a U.S. person (other than a foreign branch where the swap is conducted through such foreign branch) or be conducted through a U.S. branch,[450] and, given that the group C requirements are intended to promote counterparty protections in the context of local market sales practices, foreign regulators may have a relatively stronger supervisory interest than the Commission in regulating such swaps in relation to the group C requirements. Accordingly, the Commission stated that it believed applying the group C requirements to these transactions may not be warranted.

The Commission noted that, just as the Commission has a strong supervisory interest in regulating and enforcing the group C requirements associated with swaps taking place in the United States, foreign regulators would have a similar interest in overseeing sales practices for swaps occurring within their jurisdictions. Further, given the scope of section 2(i) of the CEA with respect to the Commission's regulation of swap activities outside the United States, the Commission stated that it believes imposing its group C requirements on a foreign-based swap between a non-U.S. swap entity or foreign branch of a U.S. swap entity, on one hand, and a foreign counterparty, on the other, is generally not necessary to advance the customer protection goals of the Dodd-Frank Act embodied in the group C requirements.

[446] Final § 23.23(e)(1)(i). The Commission notes that the addition of the Subpart L requirements to the group C requirements under the Final Rule will not substantively expand the Exchange-Traded Exception as the Subpart L requirements do not apply to swaps cleared by a DCO. Also, as stated in the Proposed Rule, the Commission considers the exception also to apply with respect to an FBOT that provides direct access to its order entry and trade matching system from within the U.S. pursuant to no-action relief issued by Commission staff.

[447] *See supra* sections III.D and IV.D.

[448] The Commission notes that, as referenced by IIB/SIFMA and subject to certain specified conditions, the Staff ITBC Letter provides relief to all swap entities from certain of the group B and group C requirements for intended to be cleared swaps.

[449] *See* Proposed Rule, 85 FR at 983–984. This approach is similar to the Guidance. *See* Guidance, 78 FR at 45360–45361. As used herein, the term swap includes transactions in swaps as well as swaps that are offered but not entered into, as applicable.

[450] *See* discussion of the modification of the definition of a ''swap conducted through a U.S. branch'' to be a ''swap booked in a U.S. branch'' in section II.H.3, *supra.*

By contrast, the Commission stated that whenever a swap involves at least one party that is a U.S. person (other than a foreign branch where the swap is conducted through such foreign branch) or is a swap conducted through a U.S. branch, the Commission believes it has a strong supervisory interest in regulating and enforcing the group C requirements, as a major purpose of Title VII is to control the potential harm to U.S. markets that can arise from risks that are magnified or transferred between parties via swaps. Therefore, the Commission concluded that exercise of U.S. jurisdiction with respect to the group C requirements over such swaps is reasonable because of the strong U.S. interest in minimizing the potential risks that may flow to the U.S. economy as a result of such swaps.[451]

(ii) Summary of Comments

ISDA stated that it fully agrees with the Commission that there is no policy benefit in subjecting non-U.S. market participants to the CFTC's extensive customer protection regime,[452] and therefore, believes that these rules should be left within the remit of home country regulators. Further, ISDA stated that it agrees that foreign branch ANE Transactions should not be subject to group C Requirements.[453] IIB/SIFMA also supported the proposed exception. However, ISDA and IIB/SIFMA requested specific changes to the underlying group C requirements, including that certain of the group C requirements apply only on an ''opt-in'' basis.

Specifically, ISDA stated that non-U.S. persons should be allowed to opt-in to receiving external business conduct disclosures from U.S. persons. Under ISDA's proposed alternative, unless a non-U.S. client chooses to ''opt-in'' into the full spectrum of the CFTC requirements, U.S swap entities and U.S. branches of non-U.S. swap entities would only have the obligation to provide disclosures related to: (1) Prohibition on fraud, manipulation, and other abusive practices; (2) verification of ECP status; (3) material risks, excluding requirements to provide daily mark and scenario analysis; (4) fair dealing communications; and (5) brief descriptions of other external business conduct disclosures, including the option to opt-in to receiving such disclosures.

IIB/SIFMA similarly requested that, to better balance counterparty protection interests against the market fragmentation that results when swap entities ask their non-U.S. counterparties to enter into documentation designed to satisfy U.S. legal requirements, the Commission refine how the group C requirements apply to all swaps entered into by U.S. swap entities and U.S. branches of non-U.S. swap entities when they transact with non-U.S. counterparties, including swaps entered into by U.S. swap entities in the United States. IIB/SIFMA argued that, because the business conduct requirements are designed to provide customer protection rather than to mitigate risk to the United States, the Commission has a limited regulatory interest in mandating full application of its customer protection requirements to all swap transactions between swap entities and their non-U.S. counterparties. Further, IIB/SIFMA asserted that, in other contexts, the Commission has recognized that non-U.S persons do not generally implicate U.S. investor protection concerns (*e.g.,* in its CPO and CTA rules). They proposed that only the following requirements would apply to a U.S. swap entity (including its U.S. branches or when it otherwise trades in the United States) or U.S. branch of a non-U.S. swap entity when it trades with a non-U.S. counterparty unless otherwise opted into by a non-U.S. person counterparty: (1) The prohibition on fraud, manipulation, and other abusive practices (but not additional confidentiality requirements under § 23.410(c)); (2) verification of ECP status (although in their view such verification should not require a written representation regarding a specific prong of the ECP definition, as it does for U.S. persons); (3) disclosure of material risks (but not scenario analysis under § 23.431(b)), material characteristics and economic terms, and material conflicts of interest and incentives (but not pre-trade mid-market marks under § 23.431(a)(3)(i)), without requiring the counterparty to agree in writing to the manner of disclosure as under § 23.402(e) and (f); (4) fair and balanced communications; and (5) a one-time notification prior to entering into a new trading relationship with a non-U.S. counterparty that the non-U.S. counterparty may opt in to the additional customer protections provided by the remaining external business conduct rules along with a summary description of those rules. Further, IIB/SIFMA requested that the Commission clarify that non-U.S. persons are not ''Special Entities'' (as defined in CEA section 4s(h)(2)(C) and § 23.401(c)), considering that Congress was not seeking to protect foreign pension plans and endowments.

(iii) Final Rule—Foreign Swap Group C Exception and U.S. Branch Group C Exception

After carefully considering the comments, the Commission is adopting the exception as proposed.[454] The Commission recognizes that, although the exception is being adopted as proposed, the scope of the exception is being expanded because the Subpart L requirements have been added to the group C requirements under the Final Rule. For the reasons discussed in section VI.A.3, the Commission believes that the Subpart L requirements are appropriately classified as group C requirements and, thus, the expansion of the exception in this manner is appropriate.

In addition, based on the comments received, the Commission is adopting an additional exception from the group C requirements for certain swaps of U.S. branches of non-U.S. swap entities (''U.S. Branch Group C Exception''), as shown in the rule text in this release.[455] Specifically, under the U.S. Branch Group C Exception, a non-U.S. swap entity is excepted from the group C requirements with respect to any swap booked in a U.S. branch with a foreign counterparty that is neither a foreign branch nor a Guaranteed Entity. The Commission is adopting this exception because, although the swaps benefiting from the exception are part of the U.S. swap market, the Commission believes that foreign regulators have a stronger interest in such swaps with respect to the group C requirements—which relate to counterparty protection rather than risk mitigation—because they are between a non-U.S. swap entity (by definition, a non-U.S. person) and certain foreign counterparties that have a limited nexus to the United States (*i.e.,* non-U.S. persons, including SRSs that are not Guaranteed Entities). The Commission is not providing this exception to swaps booked in a U.S. branch of a non-U.S. swap entity with a foreign branch of a U.S. swap entity, Guaranteed Entity, or U.S. branch counterparty (where, for the U.S. branch, the swap is booked in the U.S. branch of the counterparty). A foreign branch (which is, by definition, a part of U.S. person), a Guaranteed Entity, and a U.S. branch counterparty have a closer nexus to the United States, and,

[451] *See supra* section I.D.2.

[452] As explained more fully below, the Commission notes that it did not make such a statement in the Proposed Rule.

[453] As explained more fully below, this statement does not wholly comport with the Commission's position as set forth in the Proposed Rule.

[454] Final § 23.23(e)(1)(ii).

[455] Final § 23.23(e)(2).

thus, the Commission believes that the group C requirements should continue to apply to swaps with such counterparties.

Regarding the requests to change the application of some or all of the group C requirements to swaps entered into by U.S. swap entities and U.S. branches of non-U.S. swap entities when they transact with non-U.S. counterparties such that certain of the requirements would apply only where non-US counterparties ''opt-in'' to such treatment, the Commission is of the view that where a U.S. swap entity (other than its foreign branch) enters into a swap or where a swap is booked in a U.S. branch of a non-U.S. swap entity, those swaps are part of the U.S. swap market, and, accordingly, other than as provided in the U.S. Branch Group C Exception, the group C requirements should generally apply fully to such swap entities, regardless of the U.S. person status of its counterparty.

In response to IIB/SIFMA's comment that adopting their requested change is in line with the Commission's recognition in the CPO/CTA context that non-U.S persons do not generally implicate U.S. investor protection concerns, the Commission has never stated that U.S.-based CPOs/CTAs do not need to register or comply with the Commission's applicable rules. Rather, under § 3.10(c)(3), a foreign person is not required to register as a CPO/CTA (or comply with most Commission regulations) in connection with commodity interest transactions on behalf of persons located outside the United States that are submitted for clearing through a registered futures commission merchant. Moreover, a CPO/CTA advising a customer on the investment of their funds or managing such investment is in a fundamentally different position than a swap entity that is acting as a counterparty under a swap. In addition, as noted above, the Commission is of the view that, generally, the Final Rule is not the appropriate place to make changes to the regulation of the U.S. swap market. Making the group C requirements an ''opt-in'' regime would require changing the underlying group C requirements that apply to all covered swaps rather than creating a limited exception to them for certain foreign swaps.

On the request of IIB/SIFMA that the Commission ''clarify'' that non-U.S. persons are not Special Entities because ''Congress was not seeking to protect foreign pension plans and endowments,'' the Commission received similar comments when it adopted the definition of ''Special Entity'' in its final rule on external business conduct standards for swap entities and addressed them in that rulemaking.[456] First, the Commission, in interpreting the CEA, refined the definition of ''Special Entity'' to remove, among other things, certain foreign employee benefit plans from the scope of the definition.[457] Second, the Commission expressly addressed foreign endowments potentially being classified as Special Entities, saying that because ''the statute does not distinguish between foreign and domestic counterparties in Section 4s(h) . . . the Commission has determined that prong (v) of Section 4s(h)(2)(C) and § 23.401(c)(5) [the endowment prongs of the definitions] will apply to any endowment, whether foreign or domestic.'' [458] Therefore, the Commission is declining to provide the clarification that IIB/SIFMA requested.

Regarding ISDA's statement that it fully agrees with the Commission that there is no policy benefit in subjecting non-U.S. market participants to the CFTC's extensive customer protection regime and, therefore, believes that these rules should be left within the remit of home country regulators, this statement does not wholly comport with the Commission's position as set forth in the Proposed Rule. Rather, the Commission proposed that only certain foreign-based swaps meeting the eligibility criteria for the exception would be excepted from the group C requirements. ISDA also stated that it agrees that foreign branch ANE Transactions should not be subject to group C Requirements. The Commission notes that this would only be true to the extent the swap is conducted through the relevant foreign branch or branches, which would require, among other things, that the swap be entered into by each relevant foreign branch in its normal course of business. To satisfy this prong, it must be the normal course of business for employees located in the branch (or another foreign branch of the U.S. bank) to enter into the type of swap in question. Under the Final Rule (and as proposed), where the swap is primarily entered into by personnel not located in a foreign branch of the U.S. bank, this requirement would not be satisfied.

[456] Business Conduct Standards for Swap Dealers and Major Swap Participants With Counterparties, 77 FR 9733, 9774–75 (Feb. 2012).

[457] *Id.* at 9776.

[458] *Id.*

4. Limited Foreign Branch Group B Exception

(i) Proposed Rule

The Commission proposed that each foreign branch of a U.S. swap entity would be excepted from the group B requirements with respect to any foreign-based swap with a foreign counterparty that is an Other Non-U.S. Person, subject to certain limitations.[459] Specifically, under the Proposed Rule: (1) The exception would not be available with respect to any group B requirement for which substituted compliance (discussed in section VI.C below) is available for the relevant swap; and (2) in any calendar quarter, the aggregate gross notional amount of swaps conducted by a swap entity in reliance on the exception may not exceed five percent of the aggregate gross notional amount of all its swaps in that calendar quarter.

As discussed in the Proposed Rule, the Commission proposed the Limited Foreign Branch Group B Exception to allow the foreign branches of U.S. swap entities to continue to access swap markets for which substituted compliance may not be available under limited circumstances.[460] The Commission stated that it believes the Limited Foreign Branch Group B Exception is appropriate because U.S. swap entities' activities through foreign branches in these markets, though not significant in volume in many cases, may nevertheless be an integral element of a U.S. swap entity's global business. Additionally, although not the Commission's main purpose, the Commission noted that it endeavors to preserve liquidity in the emerging markets in which it expects this exception to be utilized, which may further encourage the global use and development of swap markets. Further, because of the proposed five percent cap on the use of the exception, the Commission stated that it preliminarily believed that the swap activity that would be excepted from the group B requirements would not raise significant supervisory concerns.

(ii) Summary of Comments

IIB/SIFMA generally supported this exception, but requested that the Commission clarify that: (1) The exception applies on a swap-by-swap,

[459] *See* Proposed Rule, 85 FR at 984. This is similar to a limited exception for transactions by foreign branches in certain specified jurisdictions in the Guidance. *See* Guidance, 78 FR at 45351.

[460] As noted above, under the Proposed Rule, where substituted compliance is available for a particular group B requirement and swap, the exception would not be available.

requirement-by-requirement basis; (2) that it is optional for a U.S. swap entity to rely on the exception for any given swap; and (3) that the five percent notional amount cap would only cover transactions entered into ''in reliance on'' the exception, not all swaps eligible for the exception. In a subsequent discussion with Commission staff, IIB/SIFMA further clarified their request that the exception should apply on a ''requirement-by-requirement basis'' to mean that the exception should have a separate five percent gross notional amount cap applicable to each requirement, rather than a single five percent gross notional amount cap where any swap that relied on the exception for any group B requirement would count towards the cap. State Street also supported the proposed exception; however, it requested that the Commission provide further guidance on the calculation of the notional amount cap.

IIB/SIFMA also asked that, consistent with its other requests, the exception be available when a foreign branch transacts with an SRS that is not a swap entity or with a U.S. branch of a foreign bank. With respect to such an entity, IIB/SIFMA noted that the group B requirements indirectly regulate the end user (*i.e.,* non-swap entity) counterparties of swap entities by requiring them to execute documentation and engage in portfolio reconciliation and compression exercises, when they trade with swap entities subject to the requirements. IIB/SIFMA asserted that many more end users will qualify as SRSs than swap entities under the proposed definition because, unlike swap entities, commercial and non-financial end users generally will not qualify for the exclusions from the SRS definition and that, as a result, significant foreign subsidiaries of large U.S. multinational companies would find themselves subject to group B requirements when they trade with non-U.S. swap entities. IIB/SIFMA noted that the indirect application of the group B requirements would pose particular problems for significant subsidiaries doing business in emerging market jurisdictions that have not yet adopted comparable rules to the group B requirements because swap entities' operations in those jurisdictions might not be set up to apply the group B requirements to trading with those subsidiaries, and that this could cause those subsidiaries to lose access to key interest or currency hedging products and face increased hedging and risk management costs relative to their foreign competitors. IIB/SIFMA also stated that subjecting an SRS that is not a swap entity to group B requirements would impose undue costs on non-U.S. swap entities, noting that because the SRS test depends on a non-U.S. counterparty's internal organizational structure and financial metrics, it generally would not be possible for a swap entity to determine whether its non-U.S. counterparty is an SRS without obtaining an affirmative representation and, because it would be difficult for a swap entity categorically to rule out any class of non-U.S. counterparties from being an SRS, swap entities would be forced to obtain relevant representations from nearly their entire global client bases.

Further, IIB/SIFMA noted that any credit or legal risks arising from swaps conducted in reliance on the exception should already be addressed through existing provisions of § 23.600 and, accordingly, they assume the Proposed Rule was not meant to imply some additional risk management program requirement in connection with reliance on the exception.

JBA asked that the Commission review the Proposed Rule from the perspective of ensuring symmetric application of requirements between U.S. swap entities and non-U.S. swap entities. Specifically, JBA requested that an exception consistent with the Limited Foreign Branch Group B Exception should be applicable to the non-U.S. swap entities even when their counterparty is a foreign branch of a U.S. person. As an example, JBA stated that when the Seoul branch of a U.S. bank that is registered as an SD enters into a swap with the Tokyo headquarters of a Japanese bank that is registered as an SD, the U.S. bank SD may rely on the Limited Foreign Branch Group B Exception, whereas the Japanese bank SD may not rely on an exception from the group B requirements.

ISDA stated that it agrees that foreign branch ANE Transactions should not be subject to group B requirements where substituted compliance is available.[461]

(iii) Final Rule

After carefully considering the comments, the Commission is adopting the exception with certain modifications, as shown in the rule text in this release.[462] Specifically, the Commission is: (1) Adjusting the exception such that it is not available for swaps between swap entities; (2) broadening the exception to apply to foreign-based swaps with an SRS End User; and (3) making some minor technical changes to the text of the Final Rule.

The Commission believes that a swap between the foreign branch of a U.S. swap entity and a non-U.S. swap entity should generally be subject to the group B requirements. Where both parties to a swap are swap entities, the rationale for the Limited Foreign Branch Group B Exception is not present. As discussed in the Proposed Rule and the Guidance, as well as above, the exception is designed to allow the foreign branches of U.S. swap entities to continue to access swap markets for which substituted compliance may not be available under limited circumstances (a) because U.S. swap entities' activities through foreign branches in these markets, though not significant in volume in many cases, may nevertheless be an integral element of a U.S. swap entity's global business, and (b) to preserve liquidity in the emerging markets in which it expects this exception to be utilized. Where both parties to a swap are registered swap entities, the Commission sees no impediment to compliance with the group B requirements.

With respect to SRS End Users, the Commission acknowledges that applying the group B requirements to a swap entity's swaps indirectly affects their counterparties, including SRS End User counterparties, by requiring them to execute documentation (*e.g.,* compliant swap trading relationship documentation), and engage in portfolio reconciliation and compression exercises as a condition to entering into swaps with swap entity counterparties. As noted by IIB/SIFMA, requiring compliance with these obligations may cause counterparties, including SRS End Users, to face increased costs relative to their competitors not affected by the application of the group B requirements (*e.g.,* for legal fees or as a result of costs being passed on to them by their swap entity counterparties), and/or to potentially lose access to key interest or currency hedging products. Also, the Commission recognizes that, as IIB/SIFMA notes, because the SRS test depends on a non-U.S. counterparty's internal organizational structure and financial metrics and it would be difficult to rule out any category of non-U.S. counterparties as being an SRS, the proposed application of group B requirements to all SRSs may cause swap entities to obtain SRS representations from nearly their entire non-U.S. client bases, potentially increasing costs for all of these clients.

[461] As discussed more fully below, this statement is not an accurate description of the Proposed Rule.

[462] Final § 23.23(e)(4).

Taking this into account and the Commission's belief that it is important to ensure that an SRS, particularly a commercial or non-financial entity, continues to have access to swap liquidity for hedging or other non-dealing purposes, the Commission is expanding the exception only to SRS End Users (and not to SRSs that are swap entities (''SRS Swap Entities'') or Guaranteed Entities). The Commission believes that an SRS End User does not pose as significant a risk to the United States as an SRS Swap Entity or a Guaranteed Entity, because an SRS End User: (1) Has a less direct connection to the United States than a Guaranteed Entity; and (2) has been involved, at most, in only a de minimis amount of swap dealing activity, or has swap positions below the MSP thresholds, such that it is not required to register as an SD or MSP, respectively. In addition, because the SRS category was first considered in the Proposed Rule, unlike for Guaranteed Entities, there is no precedent in the Guidance to apply the group B requirements to all SRSs as originally proposed. Moreover, treating SRSs End Users and Guaranteed Entities differently under the exception is consistent with the differences in swap counting requirements under the Final Rule.[463] For example, an Other Non-U.S. Person is generally not required to count a dealing swap with an SRS toward its de minimis threshold calculation for SD registration, whereas an Other Non-U.S. Person is (absent certain exceptions) generally required to count its dealing swaps with a Guaranteed Entity.

In addition, in response to commenters requesting further guidance on the application of the exception, the Commission is clarifying that the five percent gross notional amount cap applies only to swaps entered into in reliance on the exception. This does not include situations where a foreign branch of a U.S. swap entity complies with all of the group B requirements, either directly or through substituted compliance, with respect to a swap that is eligible for the exception. In such situation, though the swap is eligible for the exception for the requirements not addressed by substituted compliance, it does not count toward the five percent gross notional amount cap for swaps entered into in reliance on the exception because compliance with the applicable group B requirements was achieved. On the other hand, where a foreign branch relies on the exception with respect to any group B requirement for a swap, the notional amount of that swap counts toward the five percent gross notional amount cap for the relevant calendar quarter. The Commission is declining to expand the five percent cap as requested by IIB/SIFMA such that there would be a separate five percent gross notional amount cap for each group B requirement, because it believes such an exception would potentially allow a much greater percentage of swaps by notional amount to be eligible for the exception, and it would be difficult for a swap entity to track and for the Commission and the National Futures Association (''NFA'') to monitor compliance with such a standard. Accordingly, the five percent cap applies on a swap-by-swap basis, but does not apply on a requirement-by-requirement basis such that a foreign branch may rely on the exception for greater than five percent of its swaps by gross notional amount in any calendar quarter.

Regarding the request to expand the exception to make it available to swaps of a foreign branch with U.S. branches of foreign banks, the Commission does not believe that such an expansion is appropriate. As noted above, the exception is designed to allow the foreign branches of U.S. swap entities to continue to access swap markets for which substituted compliance may not be available under limited circumstances. It is not designed to allow foreign branches to transact with U.S. branches of non-U.S. banking organizations without complying with the group B requirements. A foreign branch of a U.S. bank is a U.S. person, and, as noted above, the Commission is of the view that where a swap is booked in a U.S. branch, that swap is part of the U.S. swap market. Accordingly, the Commission retains a supervisory interest in swaps between a foreign branch and a U.S. branch such that the group B requirements should generally apply to such swaps.

Regarding ISDA's statement that it agrees that foreign branch ANE Transactions should not be subject to group B requirements where substituted compliance is available, the Commission notes that this statement is not accurate as the Limited Foreign Branch Group B Exception does not apply where substituted compliance is available. Also, as discussed above, even where substituted compliance is not available, this statement would only be true to the extent the swap is conducted through the relevant foreign branch or branches, which would require, among other things, that the swap be entered into by each relevant foreign branch in its normal course of business. To satisfy this prong, it must be the normal course of business for employees located in the branch (or another foreign branch of the U.S. bank) to enter into the type of swap in question. Under the Final Rule (and as proposed), where the swap is primarily entered into by personnel not located in a foreign branch of the U.S. bank, this requirement would not be satisfied.

Further, in line with IIB/SIFMA's comment, the Commission confirms that its stated expectation that swap entities will address any significant risk that may arise as a result of the utilization of one or more exceptions in their risk management programs required pursuant to § 23.600 is not meant to imply an additional risk management program requirement, but rather to remind swap entities of their obligations under § 23.600.

5. Non-U.S. Swap Entity Group B Exception

(i) Proposed Rule

The Commission also proposed that each non-U.S. swap entity that is an Other Non-U.S. Person would be excepted from the group B requirements with respect to any foreign-based swap with a foreign counterparty that is also an Other Non-U.S. Person.[464] The Commission stated that, in these circumstances, where no party to the foreign-based swap is a U.S. person, a Guaranteed Entity, or an SRS, and, the particular swap is not conducted through a U.S. branch[465] of a party, notwithstanding that one or both parties to such swap may be a swap entity, the Commission believes that foreign regulators may have a relatively stronger supervisory interest in regulating such swaps with respect to the subject matter covered by the group B requirements, and that, in the interest of international comity, applying the group B requirements to these foreign-based swaps is not warranted.

The Commission noted that, generally, it would expect that swap entities that rely on this exception are subject to risk mitigation standards in the foreign jurisdictions in which they reside similar to those included in the group B requirements, as most

[463] *See* discussion of counting requirements of swaps with SRSs in sections III.B.1 and IV.B.1, *supra.*

[464] *See* Proposed Rule, 85 FR at 984. This approach is similar to the Guidance; however, the Commission notes that the Proposed Rule limited the non-U.S. swap entities eligible for this exception to those that are Other Non-U.S. Persons, and the Guidance did not contain a similar limitation. See Guidance, 78 FR at 45352–45353.

[465] *See* discussion of the modification of the definition of a ''swap conducted through a U.S. branch'' to be a ''swap booked in a U.S. branch'' in section II.H.3, *supra.*

jurisdictions surveyed by the FSB in respect of their swaps trading have implemented such standards.[466]

(ii) Summary of Comments

IIB/SIFMA agreed with the Commission that foreign regulators have a stronger supervisory interest in these swaps than the Commission in regards to the risk mitigation matters covered by the group B requirements, but recommended that the Commission expand the proposed exception by: (1) Applying the exception to swaps with an SRS that is not a swap entity, so as to avoid inappropriately burdening the foreign subsidiaries of U.S. multinational corporations and their counterparties (as discussed in section VI.B.4 above); (2) conforming the treatment of a non-U.S. swap entity that either is an SRS Swap Entity or benefits from a U.S. guarantee for the relevant swap (''Guaranteed Swap Entity'') to the Guidance[467] (or, at a minimum, adopting an exception for de minimis trading by these entities in jurisdictions not eligible for substituted compliance similar to the Limited Foreign Branch Group B Exception where, for SRS Swap Entities, the five percent notional amount cap would apply at the level of the ultimate U.S. parent entity), so as to minimize the competitive disadvantages faced by such swap entities and their counterparties when they are subject to U.S. rules extraterritorially; and (3) permitting a U.S. branch to rely on the exception when it trades with a non-U.S. person that is neither a Guaranteed Entity nor another U.S. branch, which, in their view, would appropriately recognize that such swaps do not present risks to the United States, are generally unnecessary due to home country regulation, and align the scope of the exception to be consistent with analogous EU rules.

JFMC/IBAJ similarly requested that the Commission exclude transactions between a Guaranteed Swap Entity or an SRS Swap Entity and an Other Non-U.S. Person from the application of group B requirements, stating that these requirements would not apply to such transactions under the Guidance and they see no justification for the change in Commission policy. They argued that the expanded extraterritorial application will indirectly impose regulatory compliance burdens on Japanese market participants, most of which are Other Non-U.S. Persons, when trading swaps with Guaranteed Swap Entities, especially where a Guaranteed Swap Entity cannot rely on substituted compliance with local Japanese regulations to satisfy group B requirements, and that Japanese market participants will likely refrain from trading swaps with a Guaranteed Swap Entity to avoid the indirect imposition of the Commission's swaps regulations and the costs associated therewith. They noted that this may diminish the ability of U.S.-headquartered firms to compete or access liquidity in the Japanese swaps market, which could result in fragmented global swaps markets comprised of small and disconnected liquidity pools, leading to exacerbation of systemic risk.

ISDA requested that, in line with the Proposed Rule's intent to give deference to home country regulators where there are applicable foreign regulatory requirements, the Commission not apply the proposed group B requirements to transactions between: (1) U.S. branches of non-U.S. swap entities and Other Non-U.S. Persons; and (2) Guaranteed Entities and Other Non-U.S. Persons, supporting the position and rationale of IIB/SIFMA on this topic. ISDA noted that the Commission has set a precedent for taking this approach by providing an exemption in the Guidance to Guaranteed Entities from compliance with group B requirements when transacting with Other Non-U.S. Persons.[468]

(iii) Final Rule—Non-U.S. Swap Entity Group B Exception and Limited Swap Entity SRS/Guaranteed Entity Group B Exception

After carefully considering the comments, the Commission is adopting the Non-U.S. Swap Entity Group B Exception with certain modifications, as shown in the rule text in this release.[469] Specifically, for the same reasons that the Commission is expanding the Limited Foreign Branch Group B Exception to include swaps with SRS End Users,[470] the Commission is also expanding the Non-U.S. Swap Entity Group B Exception to include swaps with SRS End Users.

In addition, based on the comments received, the Commission is adopting an additional limited exception from the group B requirements similar to the Limited Foreign Branch Group B Exception in the Final Rule (discussed above), for trading by an SRS Swap Entity or a Guaranteed Swap Entity, on the one hand, and certain non-U.S. persons, on the other (''Limited Swap Entity SRS/Guaranteed Entity Group B Exception''), as shown in the rule text in this release.[471] As commenters noted, under the Guidance, a Guaranteed Swap Entity or a non-U.S. swap entity that was a conduit affiliate would not have been expected to comply with the group B requirements when transacting with a non-U.S. person that was not a conduit or guaranteed affiliate, so the Proposed Rule deviated from the Guidance and would have disadvantaged SRS Swap Entities and Guaranteed Swap Entities relative to foreign branches of U.S. swap entities in the application of the group B requirements. Thus, the Commission believes a limited exception is warranted because, as a policy matter, it has determined that Guaranteed Swap Entities and SRS Swap Entities (who, by definition, are non-U.S. persons) should not be subject to stricter application of the group B requirements than foreign branches of U.S swap entities (who are U.S. persons). Under the Limited Swap Entity SRS/Guaranteed Entity Group B Exception, each Guaranteed Swap Entity and SRS Swap Entity is excepted from the group B requirements, with respect to any foreign-based swap with a foreign counterparty (other than a foreign branch) that is neither a swap entity[472] nor a Guaranteed Entity, subject to certain conditions. Specifically, (1) the exception is not available with respect to any group B requirement if the requirement as applicable to the swap is eligible for substituted compliance pursuant to a comparability determination issued by the Commission prior to the execution of the swap (discussed in sections VI.C and VI.D below); and (2) in any calendar quarter, the aggregate gross notional amount of swaps conducted by an SRS Swap Entity or a Guaranteed Swap Entity in reliance on this exception aggregated with the gross notional amount of swaps conducted by all affiliated SRS Swap Entities and Guaranteed Swap Entities in reliance on

[466] *See* 2019 FSB Progress Report, Table M.

[467] The Commission notes that SRSs were not contemplated by the Guidance, so the Commission assumes that the comment requested that the Commission conform the treatment of SRSs to conduit affiliates under the Guidance.

[468] The Commission assumes that ISDA was referring to non-U.S. Persons that are not a guaranteed or conduit affiliate of a U.S. Person (each as defined or described in the Guidance), as the term ''Other Non-U.S. Person'' is not used in the Guidance.

[469] Final § 23.23(e)(3).

[470] *See supra* section VI.B.4.iii.

[471] Final § 23.23(e)(5). As noted above, the Commission, generally, expects that swap entities that rely on this exception are subject to risk mitigation standards in the foreign jurisdictions in which they reside similar to those included in the group B requirements, as most jurisdictions surveyed by the FSB in respect of their swaps trading have implemented such standards. *See* 2019 FSB Progress Report, Table M.

[472] As discussed above, the Commission is also excluding swaps with a swap entity counterparty from the Limited Foreign Branch Group B Exception.

this exception does not exceed five percent of the aggregate gross notional amount of all swaps entered into by the SRS Swap Entity or a Guaranteed Swap Entity and all affiliated swap entities.[473]

With respect to the request to dis-apply fully the group B requirements to swaps between an SRS Swap Entity or Guaranteed Swap Entity, on the one hand, and an Other Non-U.S. Person on the other, the Commission believes that the group B requirements should generally continue to apply to these swaps, as these requirements relate to risk mitigation, and SRS Swap Entities and Guaranteed Swap Entities may pose significant risk to the United States. Other than the Limited Foreign Branch Group B Exception, this matches the treatment of swaps between a foreign branch of a U.S. swap entity and an Other Non-U.S. Person under the Proposed Rule. Therefore, it is the Commission's view that providing the Limited Swap Entity SRS/Guaranteed Entity Group B Exception (discussed above) to put these entities on a substantially similar footing as such foreign branches under the group B requirements under the Final Rule is the better approach.

Regarding the requests to expand the exception to include transactions between U.S. branches and certain non-U.S. persons, the Commission declines such an expansion. As noted above, the Commission believes that where a swap is booked in a U.S. branch of a non-U.S. swap entity, that swap is part of the U.S. swap market, and, accordingly, the group B requirements should generally apply.

C. Substituted Compliance

As discussed in the Proposed Rule, substituted compliance is a fundamental component of the Commission's cross-border framework.[474] It is intended to promote the benefits of integrated global markets by reducing the degree to which market participants will be subject to duplicative regulations. Substituted compliance also fosters international harmonization by encouraging U.S. and foreign regulators to adopt consistent and comparable regulatory regimes that can result in deference to each other's regime. Substituted compliance, therefore, also is consistent with the directive of Congress in the Dodd-Frank Act that the Commission ''coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation'' of swaps and swap entities.[475] When properly calibrated, substituted compliance promotes open, transparent, and competitive markets without compromising market integrity. On the other hand, if construed too broadly, substituted compliance could defer important regulatory interests to foreign regulators that have not implemented comparably robust regulatory frameworks.

The Commission has determined that, in order to achieve the important policy goals of the Dodd-Frank Act, U.S. swap entities (excluding their foreign branches) must be fully subject to the Dodd-Frank Act requirements addressed by the Final Rule, without regard to whether their counterparty is a U.S. or non-U.S. person. Given that such firms are U.S. persons conducting their business within the United States, their activities inherently have a direct and significant connection with activities in, or effect on, U.S. commerce. However, the Commission recognizes that, in certain circumstances, non-U.S. swap entities' and foreign branches' swaps with non-U.S. persons have a more attenuated nexus to U.S. commerce. Further, the Commission acknowledges that foreign jurisdictions also have a supervisory interest in such swaps. The Commission therefore believes that substituted compliance is appropriate for non-U.S. swap entities and foreign branches of U.S. swap entities in certain circumstances.

In light of the interconnectedness of the global swap market and consistent with CEA section 2(i) and principles of international comity, the Commission is implementing a substituted compliance regime with respect to the group A and group B requirements that builds upon the Commission's prior substituted compliance framework and aims to promote diverse markets without compromising the central tenets of the Dodd-Frank Act. As discussed below, the Final Rule outlines the circumstances in which a non-U.S. swap entity or foreign branch of a U.S. swap entity is permitted to comply with the group A and/or group B requirements by complying with comparable standards in its home jurisdiction.

1. Proposed Rule

The Commission proposed to permit a non-U.S. swap entity to avail itself of substituted compliance with respect to the group A requirements on an entity-wide basis.[476] The Commission also proposed to permit a non-U.S. swap entity or a foreign branch of a U.S. swap entity to avail itself of substituted compliance with respect to the group B requirements for its foreign-based swaps with foreign counterparties.[477] The Commission did not propose to permit substituted compliance for the group C requirements, where broader exceptions for swaps with foreign counterparties would be available.

2. Summary of Comments

Chatham, JFMC/IBAJ, and BGC/Tradition generally supported the Proposed Rule's approach to substituted compliance, stating that it is consistent with the principles of international comity. The Commission also received two comments requesting that the Commission expand the proposed scope of substituted compliance. Specifically, AIMA stated that the Commission should expand the availability of substituted compliance by making it available to cross-border transactions as far as possible, including any swap involving a non-U.S. person, even swaps with U.S. persons. AIMA stated that the Commission's supervisory interest in the swap activities of U.S. persons should not prelude the availability of substituted compliance for U.S. persons. AIMA also supported a universal, entity-wide approach to substituted compliance, whereby substituted compliance would be fully available for cross-border transactions.

In addition, IIB/SIFMA stated that the Commission should expand the availability of substituted compliance for the group B requirements to: (1) All swaps entered into by a non-U.S. swap entity or foreign branch, including swaps with U.S. persons; and (2) swaps conducted through a U.S. branch.[478] IIB/SIFMA further requested that the Commission make substituted compliance available for the group C requirements where such requirements apply. IIB/SIFMA noted that the SEC permits substituted compliance for U.S.-facing transactions with respect to its external business conduct standards.

[473] Final § 23.23(e)(5)(i) and (ii). As described above for the Limited Foreign Branch Group B Exception, a swap entered into by a SRS Swap Entity or Guaranteed Swap Entity will only count toward the gross notional amount cap where it is entered into in reliance on the Limited Swap Entity SRS/Guaranteed Entity Group B Exception.

[474] For example, in addition to the Guidance, the Commission has provided substituted compliance with respect to foreign futures and options transactions (*see, e.g.,* Foreign Futures and Options Transactions, 67 FR 30785 (May 8, 2002); Foreign Futures and Options Transactions, 71 FR 6759 (Feb. 9, 2006)); and margin for uncleared swaps (*see* Cross-Border Margin Rule, 81 FR 34818).

[475] *See* Dodd-Frank Act, section 752(a); 15 U.S.C. 8325.

[476] *See* Proposed § 23.23(f)(1); Proposed Rule, 85 FR at 985.

[477] *See* Proposed § 23.23(f)(2); Proposed Rule, 85 FR at 985.

[478] *See* discussion of the modification of the definition of a ''swap conducted through a U.S. branch'' to be a ''swap booked in a U.S. branch'' in section II.H.3, *supra.*

3. Final Rule

After carefully considering the comments, the Commission is adopting the scope of substituted compliance largely as proposed. The Commission continues to believe that the group A requirements, which relate to compliance programs, risk management, and swap data recordkeeping, cannot be effectively applied on a fragmented jurisdictional basis. Accordingly, it is not practical to limit substituted compliance for the group A requirements to only those transactions involving non-U.S. persons. Therefore, in furtherance of international comity, the Final Rule permits a non-U.S. swap entity, subject to the terms of the relevant comparability determination, to satisfy any applicable group A requirement on an entity-wide basis by complying with the applicable standards of a foreign jurisdiction.[479]

Unlike the group A requirements, the group B requirements, which relate to counterparty relationship documentation, portfolio reconciliation and compression, trade confirmation, and daily trading records, are more closely tied to local market conventions and can be effectively implemented on a transaction-by-transaction or relationship basis. As noted above, the Commission believes that Congress intended for the Dodd-Frank Act to apply fully to U.S. persons (other than their foreign branches) with no substituted compliance available; therefore, an expansion of substituted compliance for the group B requirements for U.S. persons is not appropriate. However, in light of the comments received, the Commission has reconsidered the availability of substituted compliance for U.S. branches of non-U.S. swap entities. In the Proposed Rule, the Commission treated a swap conducted through a U.S. branch[480] in the same manner as a swap of a U.S. swap entity for the purposes of substituted compliance. The Commission acknowledges, however, that a swap booked in a U.S. branch of a non-U.S. swap entity with a foreign counterparty that is neither a foreign branch nor a Guaranteed Entity has a comparatively smaller nexus to U.S. commerce than a swap booked in a U.S. branch with a U.S. person, Guaranteed Entity, or another U.S. branch.

Accordingly, subject to the terms of the relevant comparability determination, the Final Rule permits a non-U.S. swap entity or foreign branch of a U.S. swap entity to avail itself of substituted compliance for the group B requirements in certain circumstances, depending on the nature of its counterparty. Specifically, given the Commission's interest in promoting international comity and market liquidity, the Final Rule allows a non-U.S. swap entity or foreign branch of a U.S. swap entity, subject to the terms of the relevant comparability determination, to satisfy any applicable group B requirement for a foreign-based swap with a foreign counterparty by complying with the applicable standards of a foreign jurisdiction.[481] Further, the Final Rule allows a non-U.S. swap entity, subject to the terms of the relevant comparability determination, to satisfy any applicable group B requirement for any swap booked in a U.S. branch with a foreign counterparty that is neither a foreign branch nor a Guaranteed Entity by complying with the applicable standards of a foreign jurisdiction.[482]

The Commission is also modifying the text of § 23.23(f)(1) and (2) as shown in the rule text in this release (and including rule text in § 23.23(f)(3)) to clarify that substituted compliance is only available to a non-U.S swap entity or foreign branch of a U.S. swap entity to the extent permitted by, and subject to any conditions specified in, a comparability determination, and only where it complies with the standards of a foreign jurisdiction applicable to it, as opposed to other foreign standards to which it is not subject.[483]

With respect to the group C requirements, the Commission reiterates its longstanding position that it has a strong supervisory interest in ensuring that the counterparty protections of the group C requirements generally apply to swaps with U.S. persons with no substituted compliance available.

D. Comparability Determinations

The Commission is also implementing a process pursuant to which it will, in connection with certain requirements addressed by the Final Rule, conduct comparability determinations regarding a foreign jurisdiction's regulation of swap entities. This approach builds upon the Commission's prior substituted compliance regime and aims to promote international comity and market liquidity without compromising the Commission's interests in reducing systemic risk, increasing market transparency, enhancing market integrity, and promoting counterparty protections. Specifically, the Final Rule outlines procedures for initiating comparability determinations, including eligibility and submission requirements, with respect to certain requirements addressed by the Final Rule. The Final Rule also establishes a standard of review that the Commission will apply to such comparability determinations that emphasizes a holistic, outcomes-based approach. The Final Rule does not affect the effectiveness of any existing Commission comparability determinations that were issued consistent with the Guidance, which will remain effective pursuant to their terms.[484] The Commission may, however, reevaluate prior comparability determinations in due course pursuant to the terms of the Final Rule.

As discussed above, the Final Rule permits a non-U.S. swap entity or foreign branch of a U.S. swap entity to comply with a foreign jurisdiction's swap standards in lieu of the Commission's corresponding requirements in certain cases, provided that the Commission determines that such foreign standards are comparable to the Commission's requirements. All swap entities, regardless of whether they rely on such a comparability determination, will remain subject to the Commission's examination and enforcement authority.[485] Accordingly, if a swap entity fails to comply with a foreign jurisdiction's relevant standards, or the terms of the applicable comparability determination, the Commission may initiate an action for a violation of the Commission's corresponding requirements.

[479] Final § 23.23(f)(1).

[480] *See* discussion of the modification of the definition of a ''swap conducted through a U.S. branch'' to be a ''swap booked in a U.S. branch'' in section II.H.3, *supra.*

[481] Final § 23.23(f)(2). Thus, substituted compliance is not available for a swap booked in the U.S. branch of a non-U.S. swap entity entered into with a foreign branch of a U.S. swap entity.

[482] Final § 23.23(f)(3).

[483] Final § 23.23(f)(1) through (3).

[484] *See, e.g.,* Comparability Determination for Australia: Certain Entity-Level Requirements, 78 FR 78864 (Dec. 27, 2013); Comparability Determination for Canada: Certain Entity-Level Requirements, 78 FR 78839 (Dec. 27, 2013); Comparability Determination for the European Union: Certain Entity-Level Requirements, 78 FR 78923 (Dec. 27, 2013); Comparability Determination for Hong Kong: Certain Entity-Level Requirements, 78 FR 78852 (Dec. 27, 2013); Comparability Determination for Japan: Certain Entity-Level Requirements, 78 FR 78910 (Dec. 27, 2013); Comparability Determination for Switzerland: Certain Entity-Level Requirements, 78 FR 78899 (Dec. 27, 2013); Comparability Determination for the European Union: Certain Transaction-Level Requirements, 78 FR 78878 (Dec. 27, 2013); Comparability Determination for Japan: Certain Transaction-Level Requirements, 78 FR 78890 (Dec. 27, 2013).

[485] Final § 23.23(g)(5). The Commission notes that NFA has certain delegated authority with respect to SDs and MSPs. Additionally, all registered SDs and MSPs are required to be members of the NFA and are subject to examination by the NFA.

1. Standard of Review

(i) Proposed Rule

The Commission proposed a flexible outcomes-based approach that emphasized comparable regulatory outcomes over identical regulatory approaches. Specifically, the Commission proposed a standard of review that was designed to allow the Commission to consider all relevant elements of a foreign jurisdiction's regulatory regime, thereby permitting the Commission to tailor its assessment to a broad range of foreign regulatory approaches.[486] Accordingly, pursuant to the Proposed Rule, a foreign jurisdiction's regulatory regime did not need to be identical to the relevant Commission requirements, so long as both regulatory frameworks are comparable in terms of holistic outcome. The Proposed Rule permitted the Commission to consider any factor it deems appropriate when assessing comparability.[487]

(ii) Summary of Comments

The Commission received five comments that generally supported the proposed standard of review. However, of those commenters, JFMC/IBAJ and ISDA stated that the Commission should not consider whether a foreign jurisdiction has issued a reciprocal comparability determination in its assessment.

Further, the Commission received four comments opposing the proposed standard of review. Specifically, AFR, Better Markets, Citadel, and IATP stated that the proposed standard provides the Commission with overly-broad discretion that undermines objectivity in the assessment process. Citadel contended that the proposed standard may harm U.S. investors as a result of an overall reduction in market transparency and liquidity if trading activity is permitted to migrate to less transparent jurisdictions as a result of inaccurate comparability determinations.

IATP stated that the Commission should not base comparability on a foreign jurisdiction's supervisory guidelines or voluntary standards. IATP stated that if a foreign jurisdiction lacks a standard that compares to a Commission requirement, the Commission should issue a more limited comparability determination until such time as the foreign jurisdiction has published a standard that would result in a regulatory outcome comparable to the Commission's requirements. IATP also stated that regulatory deference to jurisdictions whose rules the Commission finds to produce regulatory outcomes comparable to those of the Commission must not be vague, unconditional, nor of indefinite duration. IATP noted that during market events or credit events, or in the event of swaps trading data anomalies, the Commission must retain the means to verify that the foreign affiliate swaps trading of U.S. parents does not result in losses that the U.S. parent must guarantee, either as a matter of law or a matter of market practice.

Citadel also recommended that the Commission provide an opportunity for public comment prior to finalizing a comparability determination to ensure that all relevant costs and benefits are considered.

(iii) Final Rule

After carefully considering the comments, the Commission is adopting the standard of review as proposed, with certain modifications as shown in the rule text in this release.[488] Specifically, the Commission is making some technical changes to the standard of review to clarify, as stated in the Proposed Rule[489] and discussed below, that the Commission may issue a comparability determination based on its determination that some or all of the relevant foreign jurisdiction's standards would result in outcomes comparable to those of the Commission's corresponding requirements or group of requirements.[490]

The Commission believes that this standard of review appropriately reflects a flexible, outcomes-based approach that emphasizes comparable regulatory outcomes over identical regulatory approaches. Accordingly, pursuant to the Final Rule, the Commission may consider any factor it deems appropriate in assessing comparability, which may include: (1) The scope and objectives of the relevant foreign jurisdiction's regulatory standards; (2) whether, despite differences, a foreign jurisdiction's regulatory standards achieve comparable regulatory outcomes to the Commission's corresponding requirements; (3) the ability of the relevant regulatory authority or authorities to supervise and enforce compliance with the relevant foreign jurisdiction's regulatory standards; and (4) whether the relevant foreign jurisdiction's regulatory authorities have entered into a memorandum of understanding or similar cooperative arrangement with the Commission regarding the oversight of swap entities.[491] In assessing comparability, the Commission need not find that a foreign jurisdiction has a comparable regulatory standard that corresponds to each group A or group B requirement. Rather, the Commission may find a foreign jurisdiction's standards comparable if, viewed holistically, the foreign jurisdiction's standards achieve a regulatory outcome that adequately serves the same regulatory purpose as the group A or group B requirements as a whole.

Further, given that some foreign jurisdictions may implement prudential supervisory guidelines in the regulation of swaps, the Final Rule allows the Commission to base comparability on a foreign jurisdiction's regulatory standards, rather than regulatory requirements. The Guidance similarly provided that the Commission has broad discretion to consider ''all relevant factors'' in assessing comparability, in addition to a non-exhaustive list of elements of comparability.[492] However, this standard of review is broader than the Guidance in that it explicitly allows the Commission to consider a foreign jurisdiction's regulatory standards (as opposed to regulatory requirements) comparable to the CEA and Commission regulations, as experience has demonstrated that such standards are often implemented in a similar manner as the Commission's swaps regime.

Although, when assessed against the relevant Commission requirements, the Commission may find comparability with respect to some, but not all, of a foreign jurisdiction's regulatory standards, it may also make a holistic finding of comparability that considers the broader context of a foreign jurisdiction's related regulatory standards. Accordingly, a comparability determination need not contain a standalone assessment of comparability for each relevant regulatory requirement, so long as it clearly indicates the scope of regulatory requirements that are covered by the determination. Further, the Commission may impose any terms and conditions on a comparability determination that it deems appropriate.[493]

The Final Rule adopts many of the Commission's existing practices with respect to comparability determinations, and does not reflect a significant change in policy. Accordingly, the phrasing of

[486] *See* Proposed § 23.23(g)(4); Proposed Rule, 85 FR at 986–987.

[487] *Id.*

[488] § 23.23(g)(4).

[489] See Proposed Rule, 85 FR at 986.

[490] *Id.*

[491] Final § 23.23(g)(4).

[492] Guidance, 78 FR at 45353.

[493] Final § 23.23(g)(6).

the standard of review is primarily intended to clarify, rather than change, the standard of review articulated in the Guidance. Reciprocity is only one of many non-determinative factors that the Commission may consider when assessing comparability. However, absence of a reciprocal comparability determination would not preclude a finding of comparability on the part of the Commission. Further, the Commission may, at its own discretion, seek public comment on any comparability determination issued pursuant to the Final Rule.

2. Supervision of Swap Entities Relying on Substituted Compliance

The Commission proposed to retain its examination and enforcement authority with respect to all swap entities relying on substituted compliance.[494] Accordingly, if a swap entity failed to comply with a foreign jurisdiction's relevant standards, or the terms of an applicable comparability determination, the Commission could initiate an action for a violation of the Commission's corresponding requirements.

IIB/SIFMA requested that the Commission state that it and NFA would not independently examine for or otherwise assess whether a swap entity is complying with foreign standards, but would instead look to the relevant foreign regulatory authority to conduct such examinations or assessments. IIB/SIFMA contended that the Commission and NFA lack the subject-matter expertise to interpret and apply foreign laws.

After carefully considering IIB/SIFMA's comment, the Commission is adopting this aspect of the rule as proposed.[495] In considering IIB/SIFMA's comment, and the broader issue of the Commission's supervision of non-U.S. swap entities, the Commission notes the various manifestations of international comity, deference, and supervisory cooperation presently taking place in the examination practices of the Commission and NFA. As a preliminary matter, the Commission's and NFA's examinations of non-U.S. swap entities occur with appropriate notice and consultation with the relevant foreign authority in the foreign jurisdiction that has primary oversight of the non-U.S swap entity. The Commission continues to be open to further ways to cooperate with such authorities in the supervision of non-U.S. swap entities.

Moreover, the Commission generally relies upon the relevant foreign regulator's oversight of a non-U.S. swap entity in relation to the application of a foreign jurisdiction's standards where a non-U.S. swap entity complies with such standards pursuant to a comparability determination issued by the Commission. To briefly recount these instances, a foreign swap entity may demonstrate compliance with a Commission requirement in group A through substituted compliance (*i.e.,* complying with comparable standards in its home jurisdiction that the Commission has determined to be comparable), regardless of whether the transactions involve a U.S. person.[496] Given the Commission's interest in promoting international comity and market liquidity, the Final Rule allows a non-U.S. swap entity (unless booking a transaction in a U.S. branch or Guaranteed Entity), or a U.S. swap entity transacting through a foreign branch, to avail itself of substituted compliance with respect to the group B requirements for swaps with foreign counterparties. Further, the Final Rule allows a non-U.S. swap entity, subject to the terms of the relevant comparability determination, to satisfy any applicable group B requirement for any swap booked in a U.S. branch with a foreign counterparty that is neither a foreign branch nor a Guaranteed Entity by complying with an applicable corresponding standard of a foreign jurisdiction. With regard to the group C requirements, the Commission considers that it is generally appropriate to defer to foreign jurisdictions and thus provides an exception from application of the business conduct standards to foreign-based swaps with foreign counterparties. The Commission has also noted above certain exceptions from the group B requirements in the Final Rule for certain foreign-based swaps; non-U.S. swap entities that avail themselves of these exceptions for their eligible swaps would only be required to comply with the applicable laws of the foreign jurisdiction(s) to which they are subject, rather than the relevant Commission requirements, for such swaps.

With regard to exams of non-U.S. swap entities and access to their books and records by the Commission and NFA, the general focus is on assessing compliance with any of the Commission's group A requirements for which substituted compliance is not found, group B requirements for transactions involving a U.S. person, and group C requirements as to transactions where the counterparty customer is in the U.S. Both the Commission and NFA retain examination and enforcement authority over swap entities to assess compliance with any Commission requirements in appropriate circumstances.[497]

3. Effect on Existing Comparability Determinations

In the Proposed Rule, the Commission stated that this rulemaking would not have any impact on the effectiveness of existing Commission comparability determinations that were issued consistent with the Guidance, which would remain effective pursuant to their terms.[498] Three commenters requested that the Commission revisit prior comparability determinations in light of this rulemaking. Specifically, ISDA stated that the Commission should recalibrate existing comparability determinations with the aim of issuing holistic, outcomes-based substituted compliance and clarify in the meantime that existing determinations would continue to be valid under the Commission's new cross-border framework. Further, IIB/SIFMA and JFMC/IBAJ requested that the Commission amend its previously-issued comparability determinations for Australia, Canada, the EU, Hong Kong, Japan, and Switzerland to include § 23.607 (antitrust requirements), which the Commission is adding to the scope of the group A requirements. The Commission has carefully considered these comments and is adopting this aspect of the rule as proposed. The Commission will consider applications to amend existing comparability determinations in due course. However, the Commission will view any previously issued comparability determination that allows for substituted compliance for § 23.201 to also allow for substituted compliance with § 45.2(a) to the extent it duplicates § 23.201.

4. Eligibility Requirements

The Proposed Rule outlined eligibility requirements to allow a comparability determination to be initiated by the Commission itself or certain outside

[494] *See* Proposed § 23.23(g)(5); Proposed Rule, 85 FR at 986. The Commission notes that it similarly retained its examination and enforcement authority in comparability determinations that were issued pursuant to the Guidance.

[495] Final § 23.23(g)(5).

[496] Moreover, to the extent a foreign swap entity receives substituted compliance for a group A requirement that incorporates § 1.31's recordkeeping requirements for certain regulatory records, § 1.31 would also not apply to such regulatory records.

[497] A non-U.S. swap entity remains subject to the Commission's anti-fraud and anti-manipulation authority, which may entail access to books and records covering transactions and/or activities not involving a U.S. person.

[498] *See* Proposed Rule, 85 FR at 986.

parties, including: (1) Swap entities that are eligible for substituted compliance; (2) trade associations whose members are such swap entities; or (3) foreign regulatory authorities that have direct supervisory authority over such swap entities and are responsible for administering the relevant swap standards in the foreign jurisdiction.[499] The Commission did not receive any comments regarding eligibility, and is therefore adopting this aspect of the rule as proposed.[500]

5. Submission Requirements

The Proposed Rule also outlined submission requirements in connection with a comparability determination with respect to some or all of the group A and group B requirements. Specifically, the Proposed Rule stated that applicants would be required to furnish certain information to the Commission that provides a comprehensive understanding of the foreign jurisdiction's relevant swap standards, including how they might differ from the corresponding requirements in the CEA and Commission regulations.[501] Further, the Proposed Rule stated that applicants would be expected to provide an explanation as to how any such differences may nonetheless achieve comparable outcomes to the Commission's attendant regulatory requirements.[502] The Commission did not receive any comments regarding submission requirements, and is therefore adopting this aspect of the rule substantially as proposed and shown in the rule text in this release.[503] Specifically, to provide the Commission additional information to use in making its comparability determinations, the Commission is revising § 23.23(g)(3)(ii) to require that the submission address how the relevant foreign jurisdiction's standards address the elements or goals of the Commission's corresponding requirements or group of requirements.[504]

VII. Recordkeeping

The Commission proposed to require a SD or MSP to create a record of its compliance with all provisions of the Proposed Rule, and retain those records in accordance with § 23.203.[505] The Commission received no comments on this provision. The Commission is therefore adopting this provision as proposed.[506] The Commission reiterates that registrants' records are a fundamental element of an entity's compliance program, as well as the Commission's oversight function. Accordingly, such records should be sufficiently detailed to allow compliance officers and regulators to assess compliance with the Final Rule.

VIII. Other Comments

The Commission received several comments that it considers beyond the scope of this rulemaking.

BGC/Tradition, IIB/SIFMA, and ISDA requested that the Commission include certain of the Unaddressed Requirements as group A requirements, group B requirements, and group C requirements.

ISDA requested that the Commission take a number of actions regarding the cross-border application of regulatory reporting requirements prior to finalizing the Proposed Rule. These included codifying an SDR reporting obligation no-action letter (CFTC Staff Letter 17–64),[507] providing substituted compliance for SDR reporting obligations for certain transactions, eliminating the Commission's large trader reporting requirements with respect to certain cross-border transactions, and revisiting the group C requirements in their entirety.

State Street recommended that the Commission address fragmentation of global non-deliverable forward liquidity pools created by Commission rulemaking and guidance in future Commission rulemaking.

JBA requested guidance on how swap requirements will apply to a non-U.S. person that is not a swap entity similar to Appendix F of the Guidance.

BGC/Tradition requested that the Commission confirm that non-U.S. introducing brokers (''IBs'') engaged in soliciting or accepting swap orders from customers, including U.S. person SDs, may comply with the applicable rules in the relevant non-U.S. jurisdictions without duplicative regulatory liability under the CEA and Commission regulations. BGC/Tradition requests that the CFTC provide guidance on how these foreign operations may avail themselves of relief through substituted compliance or another form of mutual recognition.

As noted above, these comments are beyond the scope of this rulemaking. Although not addressed in this rulemaking, the Commission appreciates the information provided by commenters and will take the requests and suggestions under advisement in the context of any relevant future Commission action.

IX. Compliance Dates and Transition Issues

A. Summary of Comments

IIB/SIFMA commented that, if adopted, the Proposed Rule would bring significant changes to portions of the Commission's cross-border framework and thus, the Commission should consider making the following clarifications and conforming changes to ensure an orderly transition process:

1. The Commission should clarify that any no-action relief or guidance that applies to the requirements not addressed in the Proposed Rule will remain effective, and that any no-action letter or guidance not specifically revoked by the Proposed Rule remains in effect.
2. If the Commission plans to amend or revoke any applicable letters, guidance, or other relief not specifically addressed in the Proposed Rule, the Commission should only do so following adequate notice and opportunity for comment.
3. The Commission should grandfather transactions entered into prior to the compliance date of any final cross-border rules adopted by the Commission.
4. The Commission should continue the codification exercise reflected by the Proposed Rule further by codifying the cross-border application of the Unaddressed Requirements.
5. The Commission should delay the compliance date for the changes set forth in the Proposed Rule until it has codified the cross-border application of the swap-related requirements not covered by the Proposed Rule. Until that time, market participants could continue to follow the Guidance.

JBA requested that the Commission clarify as soon as possible the cross-border treatment of other requirements not addressed in the Proposed Rule, and consider harmonizing the timing of application of all requirements such that they are applied simultaneously.

B. Commission Determination

As requested by IIB/SIFMA, the Commission hereby clarifies that any no-action relief or guidance that applies to the Unaddressed Requirements will remain effective, and that any no-action

[499] Proposed § 23.23(g)(2); Proposed Rule, 85 FR at 987.

[500] Final § 23.23(g)(2).

[501] Proposed § 23.23(g)(3); Proposed Rule, 85 FR at 987.

[502] Proposed § 23.23(g)(3)(iii); Proposed Rule, 85 FR at 987.

[503] Final § 23.23(g)(3).

[504] Final § 23.23(g)(3)(ii).

[505] Proposed § 23.23(h); Proposed Rule, 85 FR at 987.

[506] Final § 23.23(h)(1).

[507] CS also requested codification of CFTC Staff Letter 17–64.

letter or guidance not specifically revoked remains in effect.[508]

Regarding the scope of application of the Final Rule, as requested by commenters the Commission has provided in the Final Rule that it will only apply to swaps entered into on or after the specified compliance date.

The effective date of the Final Rule will be the date that is 60 days after publication of the Final Rule in the **Federal Register**.

The Commission has provided under paragraph (h) of the Final Rule that the exceptions provided in paragraph (e) of the Final Rule will be effective upon the effective date of the rule, provided that SDs and MSPs comply with the recordkeeping requirements set forth in paragraph (h)(1) of the Final Rule.

Otherwise, affected market participants must comply with § 23.23 on or before September 14, 2021. Given the similarity of the Final Rule to the Guidance with which market participants have been familiar since 2013, the Commission believes that a compliance period of one year is adequate for market participants to come into compliance, especially given that the Final Rule permits reliance on representations received from counterparties pursuant to the Cross-Border Margin Rule and the Guidance for many aspects of the Final Rule.

X. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act (''RFA'') requires that agencies consider whether the regulations they propose will have a significant economic impact on a substantial number of small entities.[509] In the Proposed Rule, the Commission certified that the Proposed Rule would not have a significant economic impact on a substantial number of small entities. The Commission received no comments with respect to the RFA.

The Commission previously established definitions of ''small entities'' to be used in evaluating the impact of its regulations on small entities in accordance with the RFA.[510] The Final Rule addresses when U.S. persons and non-U.S. persons are required to include their cross-border swap dealing transactions or swap positions in their SD or MSP registration threshold calculations, respectively,[511] and the extent to which SDs or MSPs are required to comply with certain of the Commission's regulations in connection with their cross-border swap transactions or swap positions.[512]

The Commission previously determined that SDs and MSPs are not small entities for purposes of the RFA.[513] The Commission believes, based on its information about the swap market and its market participants, that: (1) The types of entities that may engage in more than a de minimis amount of swap dealing activity such that they would be required to register as an SD—which generally would be large financial institutions or other large entities—would not be ''small entities'' for purposes of the RFA, and (2) the types of entities that may have swap positions such that they would be required to register as an MSP would not be ''small entities'' for purposes of the RFA. Thus, to the extent such entities are large financial institutions or other large entities that would be required to register as SDs or MSPs with the Commission by virtue of their cross-border swap dealing transactions and swap positions, they would not be considered small entities.[514]

To the extent that there are any affected small entities under the Final Rule, they would need to assess how they are classified under the Final Rule (*i.e.,* U.S. person, SRS, Guaranteed Entity, and Other Non-U.S. Person) and monitor their swap activities in order to determine whether they are required to register as an SD or MSP under the Final Rule. The Commission believes that, with the adoption of the Final Rule, market participants will only incur incremental costs, which are expected to be small, in modifying their existing systems and policies and procedures resulting from changes to the status quo made by the Final Rule.[515]

Accordingly, for the foregoing reasons, the Commission finds that there will not be a substantial number of small entities impacted by the Final Rule. Therefore, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the Final Rule will not have a significant economic impact on a substantial number of small entities.

B. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (''PRA'') [516] 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. The Final Rule provides for the cross-border application of the SD and MSP registration thresholds and the group A, group B, and group C requirements.

Commission regulations 23.23(b) and (c), which address the cross-border application of the SD and MSP registration thresholds, respectively, potentially could lead to non-U.S. persons that are currently not registered as SDs or MSPs to exceed the relevant registration thresholds, therefore requiring the non-U.S. persons to register as SDs or MSPs. However, the Commission believes that the Final Rule will not result in any new registered SDs or MSPs or the deregistration of registered SDs,[517] and therefore, it does not believe an amendment to any existing collection of information is necessary as a result of § 23.23(b) and (c). Specifically, the Commission does not believe the Final Rule will change the number of respondents under the existing collection of information, ''Registration of Swap Dealers and Major Swap Participants,'' Office of Management and Budget (''OMB'') Control No. 3038–0072.

Similarly, § 23.23(h)(1) contains collection of information requirements within the meaning of the PRA as it requires that swap entities create a record of their compliance with § 23.23 and retain records in accordance with § 23.203; however, the Commission believes that records suitable to demonstrate compliance are already required to be created and maintained under the collections related to the

[508] As noted in section V, *supra,* the ANE Staff Advisory and related ANE No-Action Relief has been withdrawn contemporaneously with promulgation of the Final Rule, while Commission staff has provided new no-action relief concerning the Unaddressed TLRs in the context of ANE Transactions.

[509] *See* 5 U.S.C. 601 *et seq.*

[510] *See* Policy Statement and Establishment of Definitions of ''Small Entities'' for Purposes of the Regulatory Flexibility Act, 47 FR 18618 (Apr. 30, 1982) (finding that DCMs, FCMs, CPOs, and large traders are not small entities for RFA purposes).

[511] Final § 23.23(b) through (d).

[512] Final § 23.23(e) through (g).

[513] *See* Entities Rule, 77 FR at 30701; Registration of Swap Dealers and Major Swap Participants, 77 FR 2613, 2620 (Jan. 19, 2012) (noting that like FCMs, SDs will be subject to minimum capital requirements, and are expected to be comprised of large firms, and that MSPs should not be considered to be small entities for essentially the same reasons that it previously had determined large traders not to be small entities).

[514] The SBA's Small Business Size Regulations, codified at 13 CFR 121.201, identifies (through North American Industry Classification System codes) a small business size standard of $38.5 million or less in annual receipts for Sector 52, Subsector 523—Securities, Commodity Contracts, and Other Financial Investments and Related Activities. Entities that are affected by the Final Rule are generally large financial institutions or other large entities that are required to include their cross-border dealing transactions or swap positions toward the SD and MSP registration thresholds, respectively, as specified in the Final Rule.

[515] The Final Rule addresses the cross-border application of the registration and certain other regulations. The Final Rule does not change such regulations.

[516] 44 U.S.C. 3501 *et seq.*

[517] There are not currently any registered MSPs.

Commission's swap entity registration, and group B and group C requirements. Specifically, existing collections of information, ''Confirmation, Portfolio Reconciliation, and Portfolio Compression Requirements for Swap Dealers and Major Swap Participants,'' OMB Control No. 3038–0068; ''Registration of Swap Dealers and Major Swap Participants,'' OMB Control No. 3038–0072; ''Swap Dealer and Major Swap Participant Conflicts of Interest and Business Conduct Standards with Counterparties,'' OMB Control No. 3038–0079; ''Confirmation, Portfolio Reconciliation, Portfolio Compression, and Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants,'' OMB Control No. 3038–0083; ''Reporting, Recordkeeping, and Daily Trading Records Requirements for Swap Dealers and Major Participants,'' OMB Control No. 3038–0087; and ''Confirmation, Portfolio Reconciliation, Portfolio Compression, and Swap Trading Relationship Documentation Requirements for Swap Dealers and Major Swap Participants,'' OMB Control No. 3038–0088 relate to these requirements.[518] Accordingly, the Commission is not submitting to OMB an information collection request to create a new information collection in relation to § 23.23(h)(1).

Final § 23.23(g) results in collection of information requirements within the meaning of the PRA, as discussed below. The Final Rule contains collections of information for which the Commission has not previously received control numbers from the OMB. Responses to this collection of information are required to obtain or retain benefits. 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 control number. The Commission has submitted to OMB an information collection request to create a new information collection under OMB control number 3038–0072 (Registration of Swap Dealers and Major Swap Participants) for the collections contained in the Final Rule.

As discussed in section VI.C above, the Commission is permitting a non-U.S. swap entity or foreign branch of a U.S. swap entity to comply with a foreign jurisdiction's swap standards in lieu of the Commission's corresponding group A and group B requirements in certain cases, provided that the Commission determines that such foreign standards are comparable to the Commission's requirements. Commission regulation 23.23(g) implements a process pursuant to which the Commission will conduct these comparability determinations, including outlining procedures for initiating such determinations. As discussed in section VI.D above, a comparability determination could be requested by swap entities that are eligible for substituted compliance, their trade associations, and foreign regulatory authorities meeting certain requirements.[519] Applicants seeking a comparability determination are required to furnish certain information to the Commission that provides a comprehensive explanation of the foreign jurisdiction's relevant swap standards, including how they might differ from the corresponding requirements in the CEA and Commission regulations and how, notwithstanding such differences, the foreign jurisdiction's swap standards achieve comparable outcomes to those of the Commission.[520] The information collection is necessary for the Commission to consider whether the foreign jurisdiction's relevant swap standards are comparable to the Commission's requirements.

Though under the Final Rule many entities are eligible to request a comparability determination,[521] the Commission expects to receive far fewer requests because once a comparability determination is made for a jurisdiction it applies for all entities or transactions in that jurisdiction to the extent provided in the Commission's determination. Further, the Commission has already issued comparability determinations under the Guidance for certain of the Commission's requirements for Australia, Canada, the European Union, Hong Kong, Japan, and Switzerland,[522] and the effectiveness of those determinations is not affected by the Final Rule. Nevertheless, in an effort to be conservative in its estimate for purposes of the PRA, the Commission estimates that it will receive a request for a comparability determination in relation to five (5) jurisdictions per year under the Final Rule. Further, based on the Commission's experience in issuing comparability determinations, the Commission estimates that each request would impose an average of 40 burden hours, for an aggregate estimated hour burden of 200 hours. Accordingly, the changes are estimated to result in an increase to the current burden estimates of OMB control number 3038–0072 by 5 in the number of submissions and 200 burden hours.

The frequency of responses and total new burden associated with OMB control number 3038–0072, in the aggregate, reflecting the new burden associated with all the amendments made by the Final Rule and current burden not affected by this Final Rule,[523] is as follows:

Estimated annual number of respondents: 770.

Estimated aggregate annual burden hours per respondent: 1.13 hours.

Estimated aggregate annual burden hours for all respondents: 872.

Frequency of responses: As needed.

Information Collection Comments. In the Proposed Rule, the Commission requested comments on the information collection requirements discussed above, including, without limitation, on the Commission's discussion of the estimated burden of the collection of information requirements in proposed § 23.23(h) (§ 23.23(h)(1) in the Final Rule). The Commission did not receive any such comments.

C. Cost-Benefit Considerations

As detailed above, the Commission is adopting rules that define certain key terms for purposes of certain Dodd-Frank Act swap provisions and that address the cross-border application of the SD and MSP registration thresholds and the Commission's group A, group B, and group C requirements.

Since issuing the Proposed Rule, the baseline against which the costs and benefits of the Final Rule are considered is unchanged and is, in principle, current law: In other words, applicable Dodd-Frank Act swap provisions in the CEA and regulations promulgated by the Commission to date, as made applicable to cross-border transactions by Congress in CEA section 2(i), in the absence of a

[518] To the extent a swap entity avails itself of an exception from a group B or group C requirement under the Final Rule and, thus, is no longer required to comply with the relevant group B and/or group C requirements and related paperwork burdens, the Commission expects the paperwork burden related to that exception would be less than that of the corresponding requirement(s). However, in an effort to be conservative, because the Commission does not know how many swap entities will choose to avail themselves of the exceptions and for how many foreign-based swaps, the Commission is not changing the burden of its related collections to reflect the availability of such exceptions.

[519] Final § 23.23(g)(2).

[520] Final § 23.23(g)(3).

[521] Currently, there are approximately 108 swap entities provisionally registered with the Commission, many of which may be eligible to apply for a comparability determination as a non-U.S. swap entity or a foreign branch. Additionally, a trade association, whose members include swap entities, and certain foreign regulators may also apply for a comparability determination.

[522] *See supra* notes 215 and 484.

[523] The numbers below reflect the current burden for two separate information collections that are not affected by this rulemaking.

Commission rule establishing more precisely the application of that provision in particular situations. However, in practice, use of this baseline poses important challenges, for a number of reasons.

First, there are intrinsic difficulties in sorting out costs and benefits of the Final Rule from costs and benefits intrinsic to the application of Dodd-Frank Act requirements to cross-border transactions directly pursuant to section 2(i), given that the statute sets forth general principles for the cross-border application of Dodd-Frank Act swap requirements but does not attempt to address particular business situations in detail.

Second, the Guidance established a general, non-binding framework for the cross-border application of many substantive Dodd-Frank Act requirements. In doing so, the Guidance considered, among other factors, the regulatory objectives of the Dodd-Frank Act and principles of international comity. As is apparent from the text of the Final Rule and the discussion in this preamble, the Final Rule is in certain respects consistent with the Guidance. The Commission understands that while the Guidance is non-binding, many market participants have developed policies and practices that take into account the views expressed therein. At the same time, some market participants may currently apply CEA section 2(i), the regulatory objectives of the Dodd-Frank Act, and principles of international comity in ways that vary from the Guidance, for example because of circumstances not contemplated by the general, non-binding framework in the Guidance.

Third, in addition to the Guidance, the Commission has issued comparability determinations finding that certain provisions of the laws and regulations of other jurisdictions are comparable in outcome to certain requirements under the CEA and regulations thereunder.[524] In general, under these determinations, a market participant that complies with the specified provisions of the other jurisdiction would also be deemed to be in compliance with Commission regulations, subject to certain conditions.[525]

Fourth, the Commission staff has issued several interpretive and no-action letters that are relevant to cross-border issues.[526] As with the Guidance, the Commission recognizes that many market participants have relied on these staff letters in framing their business practices.

Fifth, as noted above, the international regulatory landscape is far different now than it was when the Dodd-Frank Act was enacted in 2010.[527] Even in 2013, when the CFTC published the Guidance, very few jurisdictions had made significant progress in implementing the global swap reforms that were agreed to by the G20 leaders at the Pittsburgh G20 Summit. Today, however, as a result of cumulative implementation efforts by regulators throughout the world, substantial progress has been made in the world's primary swap trading jurisdictions to implement the G20 commitments. For these reasons, the actual costs and benefits of the Final Rule that are experienced by a particular market participant may vary depending on the jurisdictions in which the market participant is active and when the market participant took steps to comply with various legal requirements.

Because of these complicating factors, as well as limitations on available information, the Commission believes that a direct comparison of the costs and benefits of the Final Rule with those of a hypothetical cross-border regime based directly on section 2(i)—while theoretically the ideal approach—is infeasible in practice. As a further complication, the Commission recognizes that the Final Rule's costs and benefits would exist, regardless of whether a market participant: (1) First realized some of those costs and benefits when it conformed its business practices to provisions of the Guidance or Commission staff action that will be binding legal requirements under the Final Rule; (2) does so now for the first time; or (3) did so in stages as international requirements evolved.

In light of these considerations and given that there were no public comments regarding the baseline outlined in the Proposed Rule, the Commission has considered costs and benefits by focusing primarily on two types of information and analysis.

First, the Commission compared the Final Rule with current business practices, with the understanding that many market participants are now conducting business taking into account, among other things, the Guidance, applicable CFTC staff letters, and existing comparability determinations. This approach, for example, included a comparison of the expected costs and benefits of conducting business under the Final Rule with those of conducting business in conformance with analogous provisions of the Guidance. In effect, this analysis included an examination of new costs and benefits that will result from the Final Rule for market participants that are currently following the relevant Dodd-Frank Act swap provisions and regulations thereunder, the Guidance, the comparability determinations, the Cross-Border Margin Rule, and applicable staff letters. This is referred to as ''Baseline A.''

Second, to the extent feasible, the Commission considered relevant information on costs and benefits that market participants have incurred to date in complying with the Dodd-Frank Act in cross-border transactions of the type that will be affected by the Final Rule, absent the Guidance. This second form of analysis is, to some extent, over-inclusive in that it is likely to capture some costs and benefits that flow directly from Congress's enactment of section 2(i) of the CEA or that otherwise are not strictly attributable to the Final Rule. However, since a theoretically perfect baseline for consideration of costs and benefits does not appear feasible, this second form of analysis helps ensure that costs and benefits of the Final Rules are considered as fully as possible. This is referred to as ''Baseline B.''

The Commission requested comments regarding all aspects of the baselines applied in this consideration of costs and benefits, including a discussion of any variances or different circumstances commenters have experienced that affect the baseline for those commenters. While no commenters questioned the Commission's defined baseline, the Commission received a few cost-benefit related comments that are addressed in the relevant sections of this discussion.

The costs associated with the key elements of the Commission's cross-border approach to the SD and MSP registration thresholds—requiring market participants to classify themselves as U.S. persons, Guaranteed Entities, or SRSs[528] and to apply the rules accordingly—fall into a few categories. Market participants will incur costs determining which category of market participant they and their counterparties fall into (''assessment

[524] *See supra* notes 215 and 484.

[525] *See id.*

[526] *See, e.g.,* CFTC Letter No. 13–64, No-Action Relief: Certain Swaps by Non-U.S. Persons that are Not Guaranteed or Conduit Affiliates of a U.S. Person Not to be Considered in Calculating Aggregate Gross Notional Amount for Purposes of Swap Dealer De Minimis Exception (Oct. 17, 2013), available at *https://www.cftc.gov/idc/groups/public/@lrlettergeneral/documents/letter/13-64.pdf;* ANE Staff Advisory; ANE No-Action Relief; CFTC Staff Letter No. 18–13.

[527] *See supra* section I.C.

[528] Final § 23.23(a).

costs''), tracking their swap activities or positions to determine whether they should be included in their registration threshold calculations (''monitoring costs''), and, to the degree that their activities or positions exceed the relevant threshold, registering with the Commission as an SD or MSP (''registration costs'').

Entities required to register as SDs or MSPs as a result of the Final Rule will also incur costs associated with complying with the relevant Dodd-Frank Act requirements applicable to registrants, such as the capital, margin, and business conduct requirements (''programmatic costs'').[529] While only new registrants will assume these programmatic costs for the first time, the obligations of entities that are already registered as SDs may also change in the future as an indirect consequence of the Final Rule.

In developing the Final Rule, the Commission took into account the potential for creating or accentuating competitive disparities between market participants, which could contribute to market deficiencies, including market fragmentation or decreased liquidity, as more fully discussed below. Notably, competitive disparities may arise between U.S.-based financial groups and non-U.S. based financial groups as a result of differences in how the SD and MSP registration thresholds apply to the various classifications of market participants. For instance, an SRS must count all dealing swaps toward its SD de minimis calculation. Therefore, SRSs are more likely to trigger the SD registration threshold relative to Other Non-U.S. Persons, and may therefore be at a competitive disadvantage compared to Other Non-U.S. Persons when trading with non-U.S. persons, as non-U.S. persons may prefer to trade with non-registrants in order to avoid application of the Dodd-Frank Act swap regime.[530] On the other hand, certain counterparties may prefer to enter into swaps with SDs and MSPs that are subject to the robust requirements of the Dodd-Frank Act.

Other factors also create inherent challenges associated with attempting to assess costs and benefits of the Final Rule. To avoid the prospect of being regulated as an SD or MSP, or otherwise falling within the Dodd-Frank Act swap regime, some market participants may restructure their businesses or take other steps (*e.g.,* limiting their counterparties to Other Non-U.S. Persons) to avoid exceeding the relevant registration thresholds. The degree of comparability between the approaches adopted by the Commission and foreign jurisdictions and the potential availability of substituted compliance, whereby a market participant may comply with certain Dodd-Frank Act SD or MSP requirements by complying with a comparable requirement of a foreign financial regulator, may also affect the competitive effect of the Final Rule. The Commission expects that such effects will be mitigated as the Commission continues to work with foreign and domestic regulators to achieve international harmonization and cooperation.

In the sections that follow, the Commission discusses the costs and benefits associated with the Final Rule.[531] Section 1 discusses the main benefits of the Final Rule. Section 2 begins by addressing the assessment costs associated with the Final Rule, which derive in part from the defined terms used in the Final Rule (*e.g.,* the definitions of ''U.S. person,'' ''significant risk subsidiary,'' and ''guarantee''). Sections 3 and 4 consider the costs and benefits associated with the Final Rule's determinations regarding how each classification of market participants applies to the SD and MSP registration thresholds, respectively. Sections 5, 6, and 7 address the monitoring, registration, and programmatic costs associated with the Final Rule's cross-border approach to the SD (and, as appropriate, MSP) registration thresholds, respectively. Section 8 addresses the costs and benefits associated with the Final Rule's exceptions from, and available substituted compliance for, the group A, group B, and group C requirements, as well as comparability determinations. Section 9 addresses the costs associated with the Final Rule's recordkeeping requirements. Section 10 discusses the factors established in section 15(a) of the CEA.

1. Benefits

The main benefits of the Final Rule are two-fold: (1) Legal certainty; and (2) creating and continuing to maintain a harmonized regulatory framework internationally that shows deference to other countries' laws and regulations when such laws and regulations achieve comparable outcomes, a construct known as comity. The clarity of the Final Rule makes it easier for market participants to comply with the Commission's regulations, to conduct business in a well-organized, efficient way, and to re-allocate resources from compliance to other areas, such as productivity, business development, and innovation.

Congress directed the Commission in the Dodd-Frank Act to ''coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation'' of swaps and SDs and MSPs.[532] In doing so, the Commission is acting in the public interest and employing comity as one of the justifications for the choices the Commission is making in the Final Rule. For example, the provision of substituted compliance in the Final Rule allows some market participants to elect a regulatory jurisdiction that best suits their needs. Accordingly, some market participants may choose the U.S. as a jurisdiction in which to register and operate to achieve benefits such as robust SD requirements, third-party custodial arrangements, transparent exchanges, and bankruptcy regimes that have strong property rights and tend to lead to assets being recovered sooner than some other regimes. Therefore, the Commission believes that substituted compliance may lead to more effective regulation over time as regulators are incentivized to have their jurisdiction be chosen over other jurisdictions, and to modify ineffective or inefficient regulation as needed to adapt to market innovations and other changes that occur over time. The Commission recognizes, however, that such provision may present an opportunity for regulatory arbitrage, which could undermine the fundamental principles of the reduction of systemic risk and the promotion of market integrity.

2. Assessment Costs

As discussed above, in applying the Final Rule's cross-border approach to the SD and MSP registration thresholds,

[529] The Commission's discussion of programmatic costs and registration costs does not address MSPs. No entities are currently registered as MSPs, and the Commission does not expect that this status quo will change as a result of the Final Rule being adopted given the general similarities between the Final Rule's approach to the MSP registration threshold calculations and the Guidance.

[530] Dodd-Frank Act swap requirements may impose significant direct costs on participants falling within the SD or MSP definitions that are not borne by other market participants, including costs related to capital and margin requirements and business conduct requirements. To the extent that foreign jurisdictions adopt comparable requirements, these costs would be mitigated.

[531] The Commission endeavors to assess the expected costs and benefits of its rules in quantitative terms where possible. Where estimation or quantification is not feasible, the Commission provides its discussion in qualitative terms. Given a general lack of relevant data, the Commission's analysis in the Final Rule is generally provided in qualitative terms.

[532] *See* Dodd-Frank Act, section 752(a); 15 U.S.C. 8325.

market participants are required to first classify themselves as a U.S. person, an SRS, a Guaranteed Entity, or an Other Non-U.S. Person.

With respect to Baseline A, the Commission expects that the costs to affected market participants of assessing which classification they fall into will generally be small and incremental. In most cases, the Commission believes an entity will have performed an initial determination or assessment of its status under either the Cross-Border Margin Rule (which uses substantially similar definitions of ''U.S. person'' and ''guarantee'') or the Guidance (which interprets ''U.S. person'' in a manner that is similar but not identical to the Final Rule's definition of ''U.S. person''). Harmonizing the ''U.S. person'' definition in the Final Rule with the definition in the SEC Cross-Border Rule is also expected to reduce undue compliance costs for market participants. Additionally, the Final Rule allows market participants to rely on representations from their counterparties with regard to their classifications.[533] However, the Commission acknowledges that swap entities will have to modify their existing operations to accommodate the new concept of an SRS. Specifically, market participants must determine whether they qualify as SRSs. Further, in order to rely on certain exceptions outlined in the Final Rule, swap entities must ascertain whether they or their counterparty qualify as an SRS.

With respect to Baseline B, wherein only certain market participants have previously determined their status under the similar, but not identical, Cross-Border Margin Rule (and not the Guidance), the Commission believes that their assessment costs will nonetheless be small as a result of the Final Rule's reliance on clear, objective definitions of the terms ''U.S. person,'' ''significant risk subsidiary,'' and ''guarantee.'' Further, with respect to the determination of whether a market participant falls within the ''significant risk subsidiary'' definition,[534] the Commission believes that assessment costs are small as the definition relies, in part, on a familiar consolidation test already used by affected market participants in preparing their financial statements under U.S. GAAP. Further, only those market participants with an ultimate U.S. parent entity that has more than $50 billion in global consolidated assets and that do not fall into one of the exceptions in § 23.23(a)(13)(i) or (ii) of the Final Rule must consider if they are an SRS.

Additionally, the Final Rule primarily relies on the definition of ''guarantee'' provided in the Cross-Border Margin Rule, which is limited to arrangements in which one party to a swap has rights of recourse against a guarantor with respect to its counterparty's obligations under the swap.[535] The Final Rule also incorporates the concept of an entity with unlimited U.S. responsibility into the guarantee definition; however, the Commission is of the view that the corporate structure that this prong is designed to capture is not one that is commonly in use in the marketplace. Therefore, although non-U.S. persons must determine whether they are Guaranteed Entities with respect to the relevant swap on a swap-by-swap basis for purposes of the SD and MSP registration calculations, the Commission believes that this information is already known by non-U.S. persons.[536] Accordingly, with respect to both baselines, the Commission believes that the costs associated with assessing whether an entity or its counterparty is a Guaranteed Entity is small and incremental.

Better Markets commented that the proposed definition of ''guarantee,'' which was narrower than that in the Guidance, would increase systemic risk and hinder other public interest objectives by possibly excluding certain arrangements that may import risk into the United States. In the Proposed Rule, the Commission stated that the alignment of the definitions of ''guarantee'' in this rulemaking and the Cross-Border Margin Rule would benefit market participants to the extent that they would not be required to make a separate independent assessment of a counterparty's guarantee status. Better Markets stated that this benefit to market participants does not outweigh or reasonably approximate the potential costs to the underlying policy objectives of the Dodd-Frank Act, including promoting the safety and soundness of SDs, preventing disruptions to the derivatives markets, ensuring the financial integrity of swaps transactions and the avoidance of systemic risk, and preserving the stability of the U.S. financial system. The Commission has carefully considered the attendant costs and benefits of narrowing the definition of ''guarantee'' from the Guidance, and continues to believe, however, that the alignment of the ''guarantee'' definitions in this Final Rule and the Cross-Border Margin Rule serves to reduce costs to market participants without sacrificing the attendant policy goals of the Dodd-Frank Act. The Commission will continue to monitor arrangements that were previously considered guarantees that could shift risk back to the U.S. swap market, in general, and take appropriate action as warranted in the future.

3. Cross-Border Application of the SD Registration Threshold

(i) U.S. Persons, Guaranteed Entities, and SRSs

Under the Final Rule, a U.S. person must include all of its swap dealing transactions in its de minimis calculation, without exception.[537] As discussed above, that includes any swap dealing transactions conducted through a U.S. person's foreign branch, as such swaps are directly attributed to, and therefore affect, the U.S. person. Given that this requirement mirrors the Guidance in this respect, the Commission believes that the Final Rule will have a negligible effect on the status quo with regard to the number of registered or potential U.S. SDs, as measured against Baseline A.[538] With respect to Baseline B, all U.S. persons would have included all of their transactions in their de minimis calculation, even absent the Guidance, pursuant to paragraph (4) of the SD definition.[539] However, the Commission acknowledges that, absent the Guidance, some U.S. persons may not have interpreted CEA section 2(i) to require them to include swap dealing transactions conducted through their foreign branches in their de minimis calculation. Accordingly, with respect

[533] The Commission believes that these assessment costs for the most part have already been incurred by potential SDs and MSPs as a result of adopting policies and procedures under the Guidance and Cross-Border Margin Rule (which had similar classifications), both of which permitted counterparty representations. *See* Guidance, 78 FR at 45315; Cross-Border Margin Rule, 81 FR at 34827.

[534] The ''substantial risk subsidiary'' definition is discussed further in section II.D, *supra.*

[535] *See supra* section II.C.

[536] Because a guarantee has a significant effect on pricing terms and on recourse in the event of a counterparty default, the Commission believes that the guarantee would already be in existence and that a non-U.S. person therefore would have knowledge of its existence before entering into a swap.

[537] Final § 23.23(b)(1).

[538] The Commission is not estimating the number of new U.S. SDs, as the methodology for including swaps in a U.S. person's SD registration calculation does not diverge from the approach included in the Guidance (*i.e.,* a U.S. person must include all of its swap dealing transactions in its de minimis threshold calculation). Further, the Commission does not expect a change in the number of SDs will result from the Final Rule's definition of U.S. person and therefore assumes that no additional entities will register as U.S. SDs, and no existing U.S.-SD registrants will deregister as a result of the Final Rule.

[539] *See* 17 CFR 1.3, Swap dealer, paragraph (4).

to Baseline B, the Commission expects that some U.S. persons may incur some incremental costs as a result of having to count swaps conducted through their foreign branches.

The Final Rule also requires Guaranteed Entities to include all of their swap dealing transactions in their de minimis threshold calculation without exception.[540] This approach, which recognizes that a Guaranteed Entity's swap dealing transactions may have the same potential to affect the U.S. financial system as a U.S. person's dealing transactions, closely parallels the approach taken in the Guidance with respect to the treatment of the swaps of ''guaranteed affiliates.''[541] Given that the Final Rule establishes a more limited definition of ''guarantee'' as compared to the Guidance, and a similar definition of guarantee as compared to the Cross-Border Margin Rule, the Commission does not expect that the Final Rule will cause more Guaranteed Entities to register with the Commission. Accordingly, the Commission believes that, in this respect, any increase in costs associated with the Final Rule, with respect to Baselines A and B, will be small.

Under the Final Rule, an SRS must include all swap dealing transactions in its de minimis threshold calculation.[542] Given that the concept of an SRS was not included in the Guidance or the Cross-Border Margin Rule, the Commission believes that this aspect of the Final Rule will have a similar effect on market participants when measured against Baseline A and Baseline B. Under the Guidance, an SRS would likely have been categorized as either a conduit affiliate (which would have been required to count all dealing swaps towards its de minimis threshold calculation) or a non-U.S. person that is neither a conduit affiliate nor a guaranteed affiliate (which would have been required to count only a subset of its dealing swaps towards its de minimis threshold calculation). Accordingly, under the Final Rule, there may be some SRSs that will have to count more swaps towards their de minimis threshold calculation than would have been required under the Guidance.

However, as noted in sections II.D and III.B.1, the Commission believes that it is appropriate to distinguish SRSs from Other Non-U.S. Persons in determining the cross-border application of the SD de minimis threshold to such entities. As discussed above, SRSs, as a class of entities, present a greater supervisory interest to the CFTC relative to Other Non-U.S. Persons, due to the nature and extent of their relationships with their ultimate U.S. parent entities. Of the 61 non-U.S. SDs that were provisionally registered with the Commission as of July 2020, the Commission believes that few, if any, will be classified as SRSs pursuant to the Final Rule. With respect to Baseline A, any potential SRSs would have likely classified themselves as a conduit affiliate or a non-U.S. person that is neither a conduit affiliate nor a guaranteed affiliate pursuant to the Guidance. Accordingly, some may incur incremental costs associated with assessing and implementing the additional counting requirements for SRSs. With respect to Baseline B, the Commission believes that most potential SRSs would have interpreted section 2(i) so as to require them to count their dealing swaps with U.S. persons, but acknowledges that some may not have interpreted section 2(i) so as to require them to count swaps with non-U.S. persons toward their de minimis calculation. Accordingly, such non-U.S. persons will incur the incremental costs associated with the additional SRS counting requirements contained in the Final Rule. The Commission believes that the SRS de minimis calculation requirements will prevent regulatory arbitrage by ensuring that certain entities do not simply book swaps through a non-U.S. affiliate to avoid CFTC registration. Accordingly, the Commission believes that such provisions will benefit the swap market by ensuring that the Dodd-Frank Act swap provisions addressed by the Final Rule are applied specifically to entities whose activities, in the aggregate, have a direct and significant connection to, and effect on, U.S. commerce.

(ii) Other Non-U.S. Persons

Under the Final Rule, non-U.S. persons that are neither Guaranteed Entities nor SRSs are required to include in their de minimis threshold calculations swap dealing activities with U.S. persons (other than swaps conducted through a foreign branch of a registered SD) and certain swaps with Guaranteed Entities.[543] The Final Rule does not, however, require Other Non-U.S. Persons to include swap dealing transactions with: (1) Guaranteed Entities that are SDs; (2) Guaranteed Entities that are affiliated with an SD and are also below the de minimis threshold; (3) Guaranteed Entities that are guaranteed by a non-financial entity; (3) SRSs (other than SRSs that are also Guaranteed Entities and no other exception applies); or (4) Other Non-U.S. Persons. Additionally, Other Non-U.S. Persons are not required to include in their de minimis calculation any transaction that is executed anonymously on a DCM, registered or exempt SEF, or registered FBOT, and cleared through a registered or exempt DCO.

The Commission believes that requiring all non-U.S. persons to include their swap dealing transactions with U.S. persons in their de minimis calculations is necessary to advance the goals of the Dodd-Frank Act SD registration regime, which focuses on U.S. market participants and the U.S. market. As discussed above, the Commission believes it is appropriate to allow Other Non-U.S. Persons to exclude swaps conducted through a foreign branch of a registered SD because, generally, such swaps would be subject to Dodd-Frank Act transactional requirements and, therefore, will not evade the Dodd-Frank Act regime.

Given that these requirements are consistent with the Guidance in most respects, the Commission believes that the Final Rule will have a negligible effect on Other Non-U.S. Persons, as measured against Baseline A. With respect to Baseline B, the Commission believes that most non-U.S. persons would have interpreted CEA section 2(i) to require them to count their dealing swaps with U.S. persons, but acknowledges that some non-U.S. persons may not have interpreted 2(i) so as to require them to count such swaps with non-U.S. persons toward their de minimis calculation. Accordingly, such non-U.S. persons will incur the incremental costs associated with the counting requirements for Other Non-U.S. Persons contained in the Final Rule.

The Commission recognizes that the Final Rule's cross-border approach to

[540] Final § 23.23(b)(2)(ii).

[541] While the Final Rule and the Guidance treat swaps involving Guaranteed Entities in a similar manner, they have different definitions of the term ''guarantee.'' Under the Guidance, a ''guaranteed affiliate'' would generally include all swap dealing activities in its de minimis threshold calculation without exception. The Guidance interpreted ''guarantee'' to generally include ''not only traditional guarantees of payment or performance of the related swaps, but also other formal arrangements that, in view of all the facts and circumstances, support the non-U.S. person's ability to pay or perform its swap obligations with respect to its swaps.'' *See* Guidance, 78 FR at 45320. In contrast, the term ''guarantee'' in the Final Rule has the same meaning as defined in § 23.160(a)(2) (cross-border application of the Commission's margin requirements for uncleared swaps), except that application of the definition of ''guarantee'' in the Final Rule is not limited to uncleared swaps, and also now incorporates the concept of ''unlimited U.S. responsibility.'' *See supra* section II.C.

[542] Final § 23.23(b)(1).

[543] Final § 23.23(b)(2).

the de minimis threshold calculation could contribute to competitive disparities arising between U.S.-based financial groups and non-U.S. based financial groups. Potential SDs that are U.S. persons, SRSs, or Guaranteed Entities will be required to include all of their swap dealing transactions in their de minimis threshold calculations. In contrast, Other Non-U.S. Persons will be permitted to exclude certain dealing transactions from their de minimis calculations. As a result, Guaranteed Entities and SRSs may be at a competitive disadvantage, as more of their swap activity will apply toward the de minimis threshold (and thereby trigger SD registration) relative to Other Non-U.S. Persons.[544] While the Commission does not believe that any additional Other Non-U.S. Persons will be required to register as a SD under the Final Rule, the Commission acknowledges that to the extent that one does, its non-U.S. person counterparties (clients and dealers) may possibly cease transacting with it in order to operate outside the Dodd-Frank Act swap regime.[545] Additionally, unregistered non-U.S. dealers may be able to offer swaps on more favorable terms to non-U.S. persons than their registered competitors because they are not required to incur the costs associated with CFTC registration.[546]

As noted above, however, the Commission believes that these competitive disparities will be mitigated to the extent that foreign jurisdictions impose comparable requirements. Given that the Commission has found many foreign jurisdictions comparable with respect to various aspects of the Dodd-Frank Act swap requirements, the Commission believes that such competitive disparities will be negligible.[547] Further, as discussed below, the Commission is adopting a flexible standard of review for comparability determinations relating to the group A and group B requirements that will be issued pursuant to the Final Rule, which will serve to further mitigate any competitive disparities arising out of disparate regulatory regimes. Finally, the Commission reiterates its belief that the cross-border approach to the SD registration threshold taken in the Final Rule is appropriately tailored to further the policy objectives of the Dodd-Frank Act while mitigating unnecessary burdens and disruption to market practices to the extent possible.

(iii) Aggregation Requirement

The Final Rule also addresses the cross-border application of the aggregation requirement in a manner consistent with the Entities Rule and CEA section 2(i). Specifically, paragraph (4) of the SD definition in § 1.3 requires that, in determining whether its swap dealing transactions exceed the de minimis threshold, a person must include the aggregate notional amount of any swap dealing transactions entered into by its affiliates under common control. Consistent with CEA section 2(i), the Commission interprets this aggregation requirement in a manner that applies the same aggregation principles to all affiliates in a corporate group, whether they are U.S. or non-U.S. persons. In general, the Commission's approach allows both U.S. persons and non-U.S. persons in an affiliated group to engage in swap dealing activity up to the de minimis threshold. When the affiliated group meets the de minimis threshold in the aggregate, one or more affiliate(s) (a U.S. affiliate or a non-U.S. affiliate) have to register as an SD so that the relevant swap dealing activity of the unregistered affiliates remains below the threshold. The Commission's approach ensures that the aggregate gross notional amount of applicable swap dealing transactions of all such unregistered U.S. and non-U.S. affiliates does not exceed the de minimis level.

Given that this approach is consistent with the Guidance, the Commission believes that market participants will only incur incremental costs with respect to Baseline A in modifying their existing systems and policies and procedures in response to the Final Rule. Absent the Guidance, the Commission believes that most market participants would have relied on the interpretation of the aggregation requirement in the Entities Rule, which is similar to the approach set forth in the Final Rule. Accordingly, with respect to Baseline B, the Commission believes that market participants will only incur incremental costs in modifying their existing systems and policies and procedures in response to the Final Rule.

4. Cross-Border Application of the MSP Registration Thresholds

(i) U.S. Persons, Guaranteed Entities, and SRSs

The Final Rule's approach to the cross-border application of the MSP registration thresholds closely mirrors the approach for the SD registration threshold. Under the Final Rule, a U.S. person must include all of its swap positions in its MSP thresholds, without exception.[548] As discussed above, that includes any swap conducted through a U.S. person's foreign branch, as such swaps are directly attributed to, and therefore affect, the U.S. person. Given that this requirement is consistent with the Guidance in this respect, the Commission believes that the Final Rule will have a minimal effect on the status quo with regard to the number of potential U.S. MSPs, as measured against Baseline A. With respect to Baseline B, all of a U.S. person's swap positions would apply toward the MSP threshold calculations, even absent the Guidance, pursuant to paragraph (6) of the MSP definition.[549] However, the Commission acknowledges that, absent the Guidance, some U.S. persons may not have interpreted CEA section 2(i) to require them to include swaps conducted through their foreign branches in their MSP threshold calculations. Accordingly, with respect to Baseline B, the Commission expects that some U.S. persons may incur incremental costs as a result of having to count swaps conducted through their foreign branches.

The Final Rule also requires Guaranteed Entities to include all of their swap positions in their MSP threshold calculations without exception.[550] This approach, which recognizes that such swap transactions may have the same potential to affect the U.S. financial system as a U.S. person's swap positions, closely parallels the approach taken in the Guidance with respect to ''conduit affiliates'' and ''guaranteed affiliates.'' [551] The Commission believes that few, if any, additional MSPs will qualify as Guaranteed Entities pursuant to the Final Rule, as compared to Baseline A. Accordingly, the Commission believes that, in this

[544] On the other hand, as noted above, the Commission acknowledges that some market participants may prefer to enter into swaps with counterparties that are subject to the swaps provisions adopted pursuant to the Dodd-Frank Act. Further, Guaranteed Entities and SRSs may enjoy other competitive advantages due to the support of their guarantor or ultimate U.S. parent entity.

[545] Additionally, some unregistered dealers may opt to withdraw from the market, thereby contracting the number of dealers competing in the swaps market, which may have an adverse effect on competition and liquidity.

[546] These non-U.S. dealers also may be able to offer swaps on more favorable terms to U.S. persons, giving them a competitive advantage over U.S. competitors with respect to U.S. counterparties.

[547] *See supra* notes 215 and 484.

[548] Final § 23.23(c)(1).

[549] 17 CFR 1.3, Major swap participant, paragraph (6).

[550] Final § 23.23(c)(2)(ii).

[551] *See* Guidance, 78 FR at 45319–45320.

respect, any increase in costs associated with the Final Rule will be small.

Under the Final Rule, an SRS must also include all of its swap positions in its MSP threshold calculations.[552] Under the Guidance, an SRS would likely have been categorized as either a conduit affiliate (which would have been required to count all its swap positions towards its MSP threshold calculations) or a non-U.S. person that is neither a conduit affiliate nor a guaranteed affiliate (which would have been required to count only a subset of its swap positions towards its MSP threshold calculations). Unlike an Other Non-U.S. Person, SRSs will additionally be required to include in their MSP threshold calculations any transaction that is executed anonymously on a DCM, registered or exempt SEF, or registered FBOT, and cleared through a registered or exempt DCO.

As noted in sections II.D and IV.B.1, the Commission believes that it is appropriate to distinguish SRSs from Other Non-U.S. Persons in determining the cross-border application of the MSP thresholds to such entities, as well as with respect to the Dodd-Frank Act swap provisions addressed by the Final Rule more generally. As discussed above, SRSs, as a class of entities, present a greater supervisory interest to the CFTC relative to Other Non-U.S. Persons, due to the nature and extent of the their relationships with their ultimate U.S. parent entities. Therefore, the Commission believes that it is appropriate to require SRSs to include more of their swap positions in their MSP threshold calculations than Other Non-U.S. Persons do. Additionally, allowing an SRS to exclude all of its non-U.S. swap positions from its calculation could incentivize U.S. financial groups to book their non-U.S. positions into a non-U.S. subsidiary to avoid MSP registration requirements.

Given that this requirement was not included in the Guidance or the Cross-Border Margin Rule, the Commission believes that this aspect of the Final Rule will have a similar effect on market participants when measured against Baseline A and Baseline B. The Commission notes that there are no MSPs registered with the Commission, and expects that few entities will be required to undertake an assessment to determine whether they would qualify as an MSP under the Final Rule. Any such entities would likely have classified themselves as a non-U.S. person that is neither a conduit affiliate nor a guaranteed affiliate pursuant to the Guidance. Accordingly, they may incur incremental costs associated with assessing and implementing the additional counting requirements for SRSs. With respect to Baseline B, the Commission believes that most potential SRSs would have interpreted CEA section 2(i) to require them to count their swap positions with U.S. persons, but acknowledges that some may not have interpreted CEA section 2(i) so as to require them to count swap positions with non-U.S. persons toward their MSP threshold calculations. Accordingly, such SRSs will incur the incremental costs associated with the additional SRS counting requirements contained in the Final Rule. The Commission believes that these SRS calculation requirements will mitigate regulatory arbitrage by ensuring that U.S. entities do not simply book swaps through an SRS affiliate to avoid CFTC registration. Accordingly, the Commission believes that such provisions will benefit the swap market by ensuring that the Dodd-Frank Act swap requirements that are addressed by the Final Rule are applied to entities whose activities have a direct and significant connection to, or effect on, U.S. commerce.

(ii) Other Non-U.S. Persons

Under the Final Rule, Other Non-U.S. Persons are required to include in their MSP calculations swap positions with U.S. persons (other than swaps conducted through a foreign branch of a registered SD) and certain swaps with Guaranteed Entities.[553] The Final Rule does not, however, require Other Non-U.S. Persons to include swap positions with a Guaranteed Entity that is an SD, SRSs (other than SRSs that are also Guaranteed Entities and no other exception applies), or Other Non-U.S. Persons. Additionally, Other Non-U.S. Persons will not be required to include in their MSP threshold calculations any transaction that is executed anonymously on a DCM, a registered or exempt SEF, or registered FBOT, and cleared through a registered or exempt DCO.[554]

Given that these requirements are consistent with the Guidance in most respects, the Commission believes that the Final Rule will have a minimal effect on Other Non-U.S. Persons, as measured against Baseline A. With respect to Baseline B, the Commission believes that most non-U.S. persons would have interpreted CEA section 2(i) to require them to count their swap positions with U.S. persons, but acknowledges that some non-U.S. persons may not have interpreted CEA section 2(i) so as to require them to count swaps with non-U.S. persons toward their MSP threshold calculations. Accordingly, such non-U.S. persons will incur the incremental costs associated with the counting requirements for Other Non-U.S. Persons contained in the Final Rule.

The Commission recognizes that the Final Rule's cross-border approach to the MSP threshold calculations could contribute to competitive disparities arising between U.S.-based financial groups and non-U.S. based financial groups. Potential MSPs that are U.S. persons, SRSs, or Guaranteed Entities will be required to include all of their swap positions. In contrast, Other Non-U.S. Persons will be permitted to exclude certain swap positions from their MSP threshold calculations. As a result, SRSs and Guaranteed Entities may be at a competitive disadvantage, as more of their swap activity will apply toward the MSP calculation and trigger MSP registration relative to Other Non-U.S. Persons. While the Commission does not believe that any additional Other Non-U.S. Persons will be required to register as MSPs under the Final Rule, the Commission acknowledges that to the extent that a currently unregistered non-U.S. person is required to register as an MSP under the Final Rule, its non-U.S. person counterparties may possibly cease transacting with it in order to operate outside the Dodd-Frank Act swap regime.[555] Additionally, unregistered non-U.S. persons may be able to enter into swaps on more favorable terms to non-U.S. persons than their registered competitors because they are not required to incur the costs associated with CFTC registration.[556] As noted above, however, the Commission believes that these competitive disparities will be mitigated to the extent that foreign jurisdictions impose comparable requirements. Further, the Commission reiterates its belief that the cross-border approach to the MSP registration thresholds taken in the Final Rule aims to further the policy objectives of the Dodd-Frank Act while mitigating unnecessary burdens and disruption to market practices to the extent possible.

[552] Final § 23.23(c)(1).

[553] Final § 23.23(c)(2).

[554] Final § 23.23(d).

[555] Additionally, some unregistered swap market participants may opt to withdraw from the market, thereby contracting the number of competitors in the swaps market, which may have an effect on competition and liquidity.

[556] These non-U.S. market participants also may be able to offer swaps on more favorable terms to U.S. persons, giving them a competitive advantage over U.S. competitors with respect to U.S. counterparties.

(iii) Attribution Requirement

The Final Rule also addresses the cross-border application of the attribution requirement in a manner consistent with the Entities Rule and CEA section 2(i) and generally comparable to the approach adopted by the SEC. Specifically, the swap positions of an entity, whether a U.S. or non-U.S. person, should not be attributed to a parent, other affiliate, or guarantor for purposes of the MSP analysis in the absence of a guarantee. Even in the presence of a guarantee, attribution is not required if the entity that enters into the swap directly is subject to capital regulation by the Commission or the SEC, is regulated as a bank in the United States, or is subject to Basel compliant capital standards and oversight by a G20 prudential supervisor. The Final Rule also clarifies that the swap positions of an entity that is required to register as an MSP, or whose MSP registration is pending, is not subject to the attribution requirement. Given that this approach is largely consistent with the Guidance, with certain caveats, the Commission believes that market participants will only incur incremental costs with respect to Baseline A in modifying their existing systems and policies and procedures in response to the Final Rule. Absent the Guidance, the Commission believes that most market participants would have relied on the interpretation of the attribution requirement in the Entities Rule, which is similar to the approach set forth in the Final Rule. Accordingly, with respect to Baseline B, the Commission believes that market participants will only incur incremental costs in modifying their existing systems and policies and procedures in response to the Final Rule. In addition, the Commission believes that consistency with the approach in the SEC Cross-Border Rule will reduce compliance costs for market participants.

5. Monitoring Costs

Under the Final Rule, market participants must continue to monitor their swap activities in order to determine whether they are, or continue to be, required to register as an SD or MSP. With respect to Baseline A, the Commission believes that market participants have developed policies and practices consistent with the cross-border approach to the SD and MSP registration thresholds expressed in the Guidance. Therefore, the Commission believes that market participants will only incur incremental costs in modifying their existing systems and policies and procedures in response to the Final Rule (*e.g.,* determining which swap activities or positions are required to be included in the registration threshold calculations).[557]

For example, with respect to the SD registration threshold, SRSs may have adopted policies and practices in line with the Guidance's approach to non-U.S. persons that are not guaranteed or conduit affiliates and therefore may only be currently counting (or be provisionally registered by virtue of) their swap dealing transactions with U.S. persons, other than foreign branches of U.S. SDs. Although an SRS will be required under the Final Rule to include all dealing swaps in its de minimis calculation, the Commission believes that any increase in monitoring costs for SRSs will be negligible, both initially and on an ongoing basis, because they already have systems that track swap dealing transactions with certain counterparties in place, which includes an assessment of their counterparties' status.[558] The Commission expects that any adjustments made to these systems in response to the Final Rule will be minor.

With respect to Baseline B, the Commission believes that, absent the Guidance, most market participants would have interpreted CEA section 2(i) to require them, at a minimum, to monitor their swap activities with U.S. persons to determine whether they are, or continue to be, required to register as an SD or MSP. Accordingly, such persons will incur the incremental costs in modifying their existing systems and policies and procedures in response to the Final Rule to monitor their swap activity with certain non-U.S. persons. To the extent that market participants did not interpret CEA section 2(i) in such manner, they will incur more substantial costs in implementing such monitoring activities.

6. Registration Costs

With respect to Baseline A, the Commission believes that few, if any, additional non-U.S. persons will be required to register as an SD pursuant to the Final Rule. With respect to Baseline B, the Commission acknowledges that, absent the Guidance, some non-U.S. persons may not have interpreted CEA section 2(i) so as to require them to register with the Commission. Accordingly, a subset of such entities could be required to register with the Commission pursuant to the Final Rule.

The Commission acknowledges that if a market participant is required to register, it will incur registration costs. The Commission previously estimated registration costs in its rulemaking on registration of SDs;[559] however, the costs that may be incurred should be mitigated to the extent that any new SDs are affiliated with an existing SD, as most of these costs have already been realized by the consolidated group. While the Commission cannot anticipate the extent to which any potential new registrants will be affiliated with existing SDs, it notes that most current registrants are part of a consolidated group. The Commission has not included any discussion of registration costs for MSPs because it believes that few, if any, market participants will be required to register as an MSP under the Final Rule, as noted above.

7. Programmatic Costs

With respect to Baseline A, as noted above, the Commission believes that few, if any, additional non-U.S. persons will be required to register as an SD under the Final Rule. With respect to Baseline B, the Commission acknowledges that, absent the Guidance, some non-U.S. persons may not have interpreted CEA section 2(i) so as to require them to register with the Commission. Accordingly, a subset of such entities could be required to register with the Commission pursuant to the Final Rule.

To the extent that the Final Rule acts as a ''gating'' rule by affecting which entities engaged in cross-border swap activities must comply with the SD requirements, the Final Rule will result in increased costs for particular entities that otherwise would not register as an SD and comply with the swap requirements.[560]

8. Exceptions From Group B and Group C Requirements, Availability of Substituted Compliance, and Comparability Determinations

As discussed in section VI above, the Commission, consistent with section 2(i) of the CEA, is adopting exceptions

[557] Although the cross-border approach to the MSP registration threshold calculations in the Final Rule is not identical to the approach included in the Guidance (*see supra* section IV.B), the Commission believes that any resulting increase in monitoring costs resulting from the adoption of the Final Rule will be incremental and de minimis.

[558] *See supra* section X.C.2, for a discussion of assessment costs.

[559] *See* Registration of Swap Dealers and Major Swap Participants, 77 FR at 2623–2625.

[560] As noted above, the Commission believes that few (if any) market participants will be required to register as an MSP under the Final Rule, and therefore it has not included a separate discussion of programmatic costs for registered MSPs in this section.

from, and substituted compliance for, certain group A, group B, and group C requirements applicable to swap entities, as well as the creation of a framework for comparability determinations.

(i) Exceptions

Specifically, as discussed above in section VI, the Final Rule includes: (1) The Exchange-Traded Exception from certain group B and group C requirements for certain anonymously executed, exchange-traded, and cleared foreign-based swaps; (2) the Foreign Swap Group C Exception for certain foreign-based swaps with foreign counterparties; (3) the U.S. Branch Group C Exception, for swaps booked in a U.S. branch with certain foreign counterparties; (4) the Limited Foreign Branch Group B Exception for certain foreign-based swaps of foreign branches of U.S. swap entities with certain foreign counterparties; (5) the Non-U.S. Swap Entity Group B Exception for foreign-based swaps of non-U.S. swap entities that are Other Non-U.S. Persons with certain foreign counterparties; and (6) the Limited Swap Entity SRS/Guaranteed Entity Group B Exception for certain foreign-based swaps of SRS Swap Entities and Guaranteed Swap Entities with certain foreign counterparties.

Under the Final Rule, U.S. swap entities (other than their foreign branches) are not excepted from, or eligible for substituted compliance for, the Commission's group A, group B, and group C requirements. These requirements apply fully to registered SDs and MSPs that are U.S. persons because their swap activities are particularly likely to affect the integrity of the swap market in the United States and raise concerns about the protection of participants in those markets. With respect to both baselines, the Commission does not expect that this will impose any additional costs on market participants given that the Commission's relevant business conduct requirements already apply to U.S. SDs and MSPs pursuant to existing Commission regulations.

Pursuant to the Exchange-Traded Exception, non-U.S. swap entities and foreign branches of non-U.S. swap entities are generally excepted from most of the group B and group C requirements with respect to their foreign-based swaps that are executed anonymously on a DCM, a registered or exempt SEF, or registered FBOT, and cleared through a registered or exempt DCO.

Further, pursuant to the Foreign Swap Group C Exception, non-U.S. swap entities and foreign branches of U.S. swap entities are excepted from the group C requirements with respect to their foreign-based swaps with foreign counterparties.

Under the U.S. Branch Group C Exception, a non-U.S. swap entity is excepted from the group C requirements with respect to any swap booked in a U.S. branch with a foreign counterparty that is neither a foreign branch nor a Guaranteed Entity.

Pursuant to the Limited Foreign Branch Group B Exception, foreign branches of U.S. swap entities are excepted from the group B requirements, with respect to any foreign-based swap with a foreign counterparty that is an SRS End User or an Other Non-U.S. Person that is not a swap entity, subject to certain conditions: Specifically, (1) a group B requirement is not eligible for the exception if the requirement, as applicable to the swap, is eligible for substituted compliance pursuant to a comparability determination issued by the Commission prior to the execution of the swap; and (2) in any calendar quarter, the aggregate gross notional amount of swaps conducted by a swap entity in reliance on this exception does not exceed five percent of the aggregate gross notional amount of all its swaps.

In addition, pursuant to the Non-U.S. Swap Entity Group B Exception, non-U.S. swap entities that are Other Non-U.S. Persons are excepted from the group B requirements with respect to any foreign-based swap with a foreign counterparty that is an SRS End User or Other Non-U.S. Person.

Finally, pursuant to the Limited Swap Entity SRS/Guaranteed Entity Group B Exception, each Guaranteed Swap Entity and SRS Swap Entity is excepted from the group B requirements, with respect to any foreign-based swap with a foreign counterparty that is an SRS End User or an Other Non-U.S. Person that is not a swap entity, subject to certain conditions. Specifically, under the Final Rule: (1) The exception is not available with respect to any group B requirement if the requirement as applicable to the swap is eligible for substituted compliance pursuant to a comparability determination issued by the Commission prior to the execution of the swap; and (2) in any calendar quarter, the aggregate gross notional amount of swaps conducted by an SRS Swap Entity or a Guaranteed Swap Entity in reliance on this exception aggregated with the gross notional amount of swaps conducted by all affiliated SRS Swap Entities and Guaranteed Swap Entities in reliance on this exception does not exceed five percent of the aggregate gross notional amount of all swaps entered into by the SRS Swap Entity or a Guaranteed Swap Entity and all affiliated swap entities.

The Commission acknowledges that the group B requirements may apply more broadly to swaps between non-U.S. persons than as contemplated in the Guidance. For example, the Final Rule generally requires non-U.S. swap entities that are Guaranteed Entities or SRSs to comply with the group B requirements for swaps with Other Non-U.S. Persons, whereas the Guidance stated that all non-U.S. swap entities (other than their U.S. branches) were excluded from the group B requirements with respect to swaps with a non-U.S. person that is not a guaranteed or conduit affiliate.[561] However, the Commission believes that the exceptions from the group B requirements in the Final Rule, coupled with the availability of substituted compliance, will help to alleviate any additional burdens that may arise from such application. Further, the group C requirements have been expanded to include Subpart L, which consequently expands the scope of certain of the exceptions from the group C requirements under the Final Rule. Notwithstanding the availability of these exceptions and substituted compliance, the Commission acknowledges that some non-U.S. swap entities may incur costs to the extent that a comparability determination has not yet been issued for certain jurisdictions. Further, the Commission expects that swap entities that avail themselves of the exceptions will be able to reduce their costs of compliance with respect to the excepted requirements (which, to the extent they are similar to requirements in the jurisdiction in which they are based, may be potentially duplicative or conflicting). Swap entities are not required to take any additional action to avail themselves of these exceptions (*e.g.,* notification to the Commission) that would cause them to incur additional costs. The Commission recognizes that the exceptions (and the inherent cost savings) may give certain swap entities a competitive advantage with respect to swaps that meet the requirements of the exception.[562]

The Commission nonetheless believes that it is appropriate to tailor the application of the group B and group C

[561] The group B requirements were categorized as Category A transaction-level requirements under the Guidance.

[562] The degree of competitive disparity will depend on the degree of disparity between the Commission's requirements and that of the relevant foreign jurisdiction.

requirements in the cross-border context, consistent with section 2(i) of the CEA and international comity principles, by providing the exceptions in the Final Rule. In doing so, the Commission is aiming to reduce market fragmentation which may result by applying certain duplicative swap requirements in non-U.S. markets, which are often subject to robust foreign regulation. Other than the U.S. Branch Group C Exception, the exceptions in the Final Rule are largely similar to those provided in the Guidance. Therefore, the Commission does not expect that the exceptions in the Final Rule will, in the aggregate, have a significant effect on the costs of, and benefits to, swap entities.

(ii) Substituted Compliance

As described in section VI.C, the extent to which substituted compliance is available under the Final Rule depends on the classification of the swap entity or branch and, in certain cases the counterparty, to a particular swap. The Commission recognizes that the decision to offer substituted compliance carries certain trade-offs. Given the global and highly-interconnected nature of the swap market, where risk is not bound by national borders, market participants are likely to be subject to the regulatory interest of more than one jurisdiction. Allowing compliance with foreign swap standards as an alternative to compliance with the Commission's requirements can therefore reduce the application of duplicative or conflicting requirements, resulting in lower compliance costs and potentially facilitating a more efficient regulatory framework over time. Substituted compliance also helps preserve the benefits of an integrated, global swap market by fostering and advancing efforts among U.S. and foreign regulators to collaborate in establishing robust regulatory standards. If substituted compliance is not properly implemented, however, the Commission's swap regime could lose some of its effectiveness. Accordingly, the ultimate costs and benefits of substituted compliance are affected by the standard under which it is granted and the extent to which it is applied. The Commission was mindful of this dynamic in structuring a substituted compliance regime for the group A and group B requirements and has determined that the Final Rule will enhance market efficiency and foster global coordination of these requirements while ensuring that swap entities (wherever located) are subject to comparable regulation.

The Commission also understands that by not offering substituted compliance equally to all swap entities, the Final Rule could lead to certain competitive disparities between swap entities. For example, to the extent that a non-U.S. swap entity can rely on substituted compliance that is not available to a U.S. swap entity, it may enjoy certain cost advantages (*e.g.,* avoiding the costs of potentially duplicative or inconsistent regulation). The non-U.S. swap entity may then be able to pass on these cost savings to its counterparties in the form of better pricing or some other benefit. U.S. swap entities, on the other hand, could, depending on the extent to which foreign swap requirements apply, be subject to both U.S. and foreign requirements, and therefore be at a competitive disadvantage. Counterparties may also be incentivized to transact with swap entities that are offered substituted compliance in order to avoid being subject to duplicative or conflicting swap requirements, which could lead to increased market deficiencies.[563]

Nevertheless, the Commission does not believe it is appropriate to make substituted compliance broadly available to all swap entities because it needs to protect market participants and the public. As discussed above, the Commission has a strong supervisory interest in the swap activity of all swap entities, including non-U.S. swap entities, by virtue of their registration with the Commission. Further, U.S. swap entities are particularly key swap market participants, and their safety and soundness is critical to a well-functioning U.S. swap market and the stability of the U.S. financial system. The Commission believes that losses arising from the default of a U.S. entity are more likely to be borne by other U.S. entities (including parent companies); therefore, a U.S. entity's risk to the U.S. financial system is more acute than that of a similarly situated non-U.S. entity. Accordingly, in light of the Commission's supervisory interest in the activities of U.S. persons and its statutory obligation to ensure the safety and soundness of swap entities and the U.S. swap market, the Commission believes that it is generally not appropriate for substituted compliance to be available to U.S. swap entities for purposes of the Final Rule. With respect to non-U.S. swap entities, however, the Commission believes that, in the interest of international comity, making substituted compliance generally available for the requirements discussed in the Final Rule is appropriate.

IATP stated that the Commission should not make the costs of complying with, or economic benefits from, substituted compliance a decision criterion for comparability determinations, and that participation in U.S. markets is a privilege with consequent costs and benefits. Such costs and benefits drive the underlying policy of the substituted compliance regime as discussed in this Final Rule, rather than the decision-making that accompanies an individual comparability determination assessment.

(iii) Comparability Determinations

As noted in section VI.D above, under the Final Rule, a comparability determination may be requested by: (1) Eligible swap entities; (2) trade associations whose members are eligible swap entities; or (3) foreign regulatory authorities that have direct supervisory authority over eligible swap entities and are responsible for administering the relevant foreign jurisdiction's swap requirements.[564] Once a comparability determination is made for a jurisdiction, it applies for all entities or transactions in that jurisdiction to the extent provided in the determination, as approved by the Commission.[565] Accordingly, given that the Final Rule will have no effect on any existing comparability determinations, swap entities may continue to rely on such determinations with no effect on the costs or benefits of such reliance. To the extent that an entity wishes to request a new comparability determination pursuant to the Final Rule, it will incur costs associated with the preparation and filing of a submission request. However, the Commission anticipates that a person would not elect to incur the costs of submitting a request for a comparability determination unless such costs were exceeded by the cost savings associated with substituted compliance.

The Final Rule includes a standard of review that allows for a holistic, outcomes-based approach that enables the Commission to consider any factor it deems relevant in assessing comparability. Further, in determining whether a foreign regulatory standard is comparable to a corresponding Commission requirement, the Final Rule

[563] The Commission recognizes that its substituted compliance framework may impose certain initial operational costs, as in certain cases swap entities will be required to determine the status of their counterparties in order to determine the extent to which substituted compliance is available.

[564] Final § 23.23(g)(2).

[565] Final § 23.23(f).

allows the Commission to consider the broader context of a foreign jurisdiction's related regulatory requirements. Allowing for a comparability determination to be made based on comparable outcomes, notwithstanding potential differences in foreign jurisdictions' relevant standards, helps to ensure that substituted compliance is made available to the fullest extent possible. While the Commission recognizes that, to the extent that a foreign swap regime is not deemed comparable in all respects, swap entities eligible for substituted compliance may incur costs from being required to comply with more than one set of specified swap requirements, the Commission believes that this approach is preferable to an all-or-nothing approach, in which market participants may be forced to comply with both regimes in their entirety.

9. Recordkeeping

The Final Rule also requires swap entities to create and retain records of their compliance with the Final Rule.[566] Given that swap entities are already subject to robust recordkeeping requirements, the Commission believes that swap entities will only incur incremental costs, which are expected to be minor, in modifying their existing systems and policies and procedures resulting from changes to the status quo made by the Final Rule.

10. Alternatives Considered

The Commission carefully considered several alternatives to various provisions of the Final Rule. In determining whether to accept or reject each alternative, the Commission considered the potential costs and benefits associated with each alternative.

For example, the Commission considered Better Markets' suggestion that the Commission add two additional tests to determine whether an entity is a significant subsidiary. Better Markets proposed that if an entity were to meet a risk transfer test, measuring the notional amount of swaps that are back-to-backed with U.S. entities, or a risk acceptance test, measuring the trading activity of the subsidiary over a three month time period, then the entity should be considered a significant subsidiary. The Commission declined to include these two tests because these activity-based tests do not provide a measure of risk that a subsidiary poses to a parent entity, and thus would potentially subject a greater number of entities to certain Commission regulations without providing a significant reduction in systemic risk.

Similarly, the Commission considered IIB/SIFMA's comment that the application of the group B requirements to swaps of Guaranteed Swap Entities and SRS Swap Entities should conform to the Guidance, so as to reduce the competitive disadvantages faced by such swap entities and their counterparties when they are subject to U.S. rules extraterritorially. The Commission declined to adopt this alternative, citing the fact that the group B requirements relate to risk mitigation, and SRS Swap Entities and Guaranteed Swap Entities may pose significant risk to the United States. However, the Commission acknowledged the potential competitive disadvantages that such application may pose to Guaranteed Swap Entities and SRS Swap Entities (as opposed to foreign branches of U.S. swap entities), and therefore also adopted the Limited Swap Entity SRS/Guaranteed Entity Group B Exception in an effort to reduce potential burdens to such entities without sacrificing the important risk mitigation goals associated with the group B requirements.

On the other hand, the Commission adopted certain alternatives to elements of the Proposed Rule. For example, CS and IIB/SIFMA stated that the exclusion for subsidiaries of BHCs in the SRS definition should be expanded to include those entities that are subsidiaries of IHCs. These commenters noted that IHCs are subject to prudential regulation, including Basel III capital requirements, stress testing, liquidity, and risk management requirements. The Commission determined that IHCs are subject to prudential standards by the Federal Reserve Board that are similar to those to which BHCs are subject. In general, IHCs and BHCs of similar size are subject to similar liquidity, risk management, stress testing, and credit limit standards. Therefore, for the same risk-based reasons that the Commission proposed to exclude subsidiaries of BHCs from the definition of SRS, the Commission is expanding the SRS exclusion to include subsidiaries of both BHCs and IHCs in § 23.23(a)(13)(i).

The Commission is also adopting an alternative raised by IIB/SIFMA, who recommended that the Commission expand the proposed Non-U.S. Swap Entity Group B Exception and the Limited Foreign Branch Group B Exception by applying the exceptions to swaps with an SRS that is not a swap entity, so as to avoid inappropriately burdening the foreign subsidiaries of U.S. multinational corporations and their counterparties. In doing so, the Commission acknowledges that applying the group B requirements to a swap entity's swaps indirectly affects their counterparties, including SRS End User counterparties, by requiring them to execute documentation (*e.g.,* compliant swap trading relationship documentation), and engage in portfolio reconciliation and compression exercises as a condition to entering into swaps with swap entity counterparties. Accordingly, mandating compliance with these obligations may cause counterparties, including SRS End Users, to face increased costs relative to their competitors not affected by the application of the group B requirements (*e.g.,* for legal fees or as a result of costs being passed on to them by their swap entity counterparties) and/or to potentially lose access to key interest rate or currency hedging products. Also, because the SRS test depends on a non-U.S. counterparty's internal organizational structure and financial metrics and it would be difficult to rule out any category of non-U.S. counterparties as being an SRS, the proposed application of group B requirements to all SRSs may cause swap entities to obtain SRS representations from nearly their entire non-U.S. client bases, potentially increasing costs for all of these clients.

In light of the importance of ensuring that an SRS, particularly a commercial or non-financial entity, continues to have access to swap liquidity for hedging or other non-dealing purposes, the Commission expanded the exceptions to apply to SRS End Users. The Commission noted that an SRS End User does not pose as significant a risk to the United States as an SRS Swap Entity or a Guaranteed Entity, because an SRS End User: (1) Has a less direct connection to the United States than a Guaranteed Entity; and (2) has been involved, at most, in only a de minimis amount of swap dealing activity, or has swap positions below the MSP thresholds, such that it is not required to register as a SD or MSP, respectively.

The Commission considered several other alternatives to the Final Rule, which are discussed in detail throughout this release.[567] In each instance, the Commission considered the costs and burdens of the Final Rule and the regulatory benefits that the Final Rule seeks to achieve.

11. Section 15(a) Factors

Section 15(a) of the CEA[568] requires the Commission to consider the costs and benefits of its actions before

[566] Final § 23.23(h)(1).

[567] *See supra* sections II–VI.

[568] 7 U.S.C. 19(a).

promulgating a regulation under the CEA or issuing certain orders. Section 15(a) further specifies that the 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 considers the costs and benefits resulting from its discretionary determinations with respect to the section 15(a) factors.

(i) Protection of Market Participants and the Public

The Commission believes the Final Rule will support protection of market participants and the public. By focusing on and capturing swap dealing transactions and swap positions involving U.S. persons, SRSs, and Guaranteed Entities, the Final Rule's approach to the cross-border application of the SD and MSP registration threshold calculations works to ensure that, consistent with CEA section 2(i) and the policy objectives of the Dodd-Frank Act, significant participants in the U.S. market are subject to these requirements. The cross-border approach to the group A, group B, and group C requirements similarly ensures that these requirements apply to swap activities that are particularly likely to affect the integrity of, and raise concerns about, the protection of participants in the U.S. market while, consistent with principles of international comity, recognizing the supervisory interests of the relevant foreign jurisdictions in applying their own requirements to transactions involving non-U.S. swap entities and foreign branches of U.S. swap entities with non-U.S. persons and foreign branches of U.S. swap entities.

(ii) Efficiency, Competitiveness, and Financial Integrity of the Markets

To the extent that the Final Rule leads additional entities to register as SDs or MSPs, the Commission believes that the Final Rule will enhance the financial integrity of the markets by bringing significant U.S. swap market participants under Commission oversight, which may reduce market disruptions and foster confidence and transparency in the U.S. market. The Commission recognizes that the Final Rule's cross-border approach to the SD and MSP registration thresholds may create competitive disparities among market participants, based on the degree of their connection to the United States, that could contribute to market deficiencies, including market fragmentation and decreased liquidity, as certain market participants may reduce their exposure to the U.S. market. As a result of reduced liquidity, counterparties may pay higher prices, in terms of bid-ask spreads. Such competitive effects and market deficiencies may, however, be mitigated by global efforts to harmonize approaches to swap regulation and by the large inter-dealer market, which may link the fragmented markets and enhance liquidity in the overall market. The Commission believes that the Final Rule's approach is necessary and appropriately tailored to ensure that the purposes of the Dodd-Frank Act swap regime and its registration requirements are advanced while still establishing a workable approach that recognizes foreign regulatory interests and reduces competitive disparities and market deficiencies to the extent possible. The Commission further believes that the Final Rule's cross-border approach to the group A, group B, and group C requirements will promote the financial integrity of the markets by fostering transparency and confidence in the significant participants in the U.S. swap markets.

(iii) Price Discovery

The Commission recognizes that the Final Rule's approach to the cross-border application of the SD and MSP registration thresholds and group A, group B, and group C requirements could have an effect on liquidity, which may in turn influence price discovery. As liquidity in the swap market is lessened and fewer dealers compete against one another, bid-ask spreads (cost of swap and cost to hedge) may widen and the ability to observe an accurate price of a swap may be hindered. However, as noted above, these negative effects will be mitigated as jurisdictions harmonize their swap regimes and global financial institutions continue to manage their swap books (*i.e.,* moving risk with little or no cost, across an institution to market centers, where there is the greatest liquidity). The Commission does not believe that the Final Rule's approach to the group A, group B, and group C requirements will have a noticeable effect on price discovery.

(iv) Sound Risk Management Practices

The Commission believes that the Final Rule's approach could promote the development of sound risk management practices by ensuring that significant participants in the U.S. market are subject to Commission oversight (via registration), including in particular important counterparty disclosure and recordkeeping requirements that will encourage policies and practices that promote fair dealing while discouraging abusive practices in U.S. markets. On the other hand, to the extent that a registered SD or MSP relies on the exceptions in the Final Rule, and is located in a jurisdiction that does not have comparable swap requirements, the Final Rule could lead to weaker risk management practices for such entities.

(v) Other Public Interest Considerations

The Commission believes that the Final Rule is consistent with principles of international comity. The Commission has carefully considered, among other things, the level of foreign jurisdictions' supervisory interests over the subject activity and the extent to which the activity takes place within a particular foreign territory. In doing so, the Commission has strived to minimize conflicts with the laws of other jurisdictions while seeking, pursuant to section 2(i), to apply the swaps requirements of the Dodd-Frank Act to activities outside the United States that have a direct and significant connection with activities in, or effect on, U.S. commerce.

The Commission believes the Final Rule appropriately accounts for these competing interests, ensuring that the Commission can discharge its responsibilities to protect the U.S. markets, market participants, and financial system, consistent with international comity. Of particular relevance is the Commission's approach to substituted compliance in the Final Rule, which mitigates burdens associated with potentially duplicative foreign laws and regulations in light of the supervisory interests of foreign regulators in entities domiciled and operating in their own jurisdictions.

D. Antitrust Laws

Section 15(b) of the CEA requires the Commission to take into consideration the public interest to be protected by the antitrust laws and endeavor to take the least anticompetitive means of achieving the objectives of the CEA, as well as the policies and purposes of the CEA, in issuing any order or adopting any Commission rule or regulation (including any exemption under section 4(c) or 4c(b)), or in requiring or approving any bylaw, rule, or regulation of a contract market or registered futures association established pursuant to section 17 of the CEA.[569]

[569] 7 U.S.C. 19(b).

The Commission believes that the public interest to be protected by the antitrust laws is generally to protect competition. The Commission requested and did not receive any comments on whether the Proposed Rule implicated any other specific public interest to be protected by the antitrust laws.

The Commission has considered the Final Rule to determine whether it is anticompetitive and has identified no significant discretionary anticompetitive effects.[570] The Commission requested and did not receive any comments on whether the Proposed Rule was anticompetitive and, if it was, what the anticompetitive effects are.

Because the Commission has determined that the Final Rule is not anticompetitive and has no significant discretionary anticompetitive effects and received no comments on its determination on the Proposed Rule, the Commission has not identified any less anticompetitive means of achieving the purposes of the CEA.

XI. Preamble Summary Tables

A. Table A—Cross-Border Application of the SD De Minimis Threshold

Table A should be read in conjunction with the text of the Final Rule.

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Potential SD ↓ / Counterparty →		U.S. Person	Non-U.S. Person		
			Guaranteed Entity	SRS	Other Non-U.S. Person
U.S. Person		Include	Include	Include	Include
Non-U.S. Person	Guaranteed Entity	Include	Include	Include	Include
	SRS	Include	Include	Include	Include
	Other Non-U.S. Person[1]	Include[2]	Include[3]	Exclude	Exclude

[1] Does not include swaps entered into anonymously on a DCM, a registered SEF or a SEF exempted from registration, or a registered FBOT and cleared through a registered DCO or a DCO exempted from registration.
[2] Unless the swap is conducted through a foreign branch of a registered SD.
[3] Unless the Guaranteed Entity is registered as an SD, unless the guarantor is a non-financial entity, or unless the Guaranteed Entity is itself below the de minimis threshold and is affiliated with a registered SD.

B. Table B—Cross-Border Application of the MSP Threshold

Table B should be read in conjunction with the text of the Final Rule.

[570] The Final Rule is being adopted pursuant to the direction of Congress in section 2(i) of the CEA, as discussed in section I.D, that the swap provisions of the CEA enacted by Title VII of the Dodd-Frank Act, including any rule prescribed or regulation promulgated under the CEA, shall not apply to activities outside the United States unless those activities have a direct and significant connection with activities in, or effect on, commerce of the United States, or they contravene Commission rules or regulations as are necessary or appropriate to prevent evasion of the swap provisions of the CEA enacted under Title VII. As discussed above, the degree of any competitive disparity will depend on the degree of disparity between the Commission's requirements and that of the relevant foreign jurisdiction.

Counterparty → / Potential MSP ↓		U.S. Person	Non-U.S. Person		
			Guaranteed Entity	SRS	Other Non-U.S. Person
U.S. Person		Include	Include	Include	Include
Non-U.S. Person	Guaranteed Entity	Include	Include	Include	Include
	SRS	Include	Include	Include	Include
	Other Non-U.S. Person[1]	Include[2]	Include[3]	Exclude	Exclude

[1] Does not include swap positions entered into anonymously on a DCM, a registered SEF or a SEF exempted from registration, or a registered FBOT and cleared through a registered DCO or a DCO exempted from registration.
[2] Unless the swap is conducted through a foreign branch of a registered SD.
[3] Unless the Guaranteed Entity is registered as an SD.

Additionally, all swap positions that are subject to recourse should be attributed to the guarantor, whether it is a U.S. person or a non-U.S. person, unless the guarantor, the Guaranteed Entity, and its counterparty are Other Non-U.S. Persons.

C. Table C—Cross-Border Application of the Group B Requirements in Consideration of Related Exceptions and Substituted Compliance

Table C[571] should be read in conjunction with the text of the Final Rule.

[571] As discussed in section VI.A.2, *supra,* the group B requirements are set forth in §§ 23.202, 23.501, 23.502, 23.503, and 23.504 and relate to (1) swap trading relationship documentation; (2) portfolio reconciliation and compression; (3) trade confirmation; and (4) daily trading records. Exceptions from the group B requirements are discussed in sections VI.B.2, VI.B.4, and VI.B.5, *supra.* Substituted compliance for the group B requirements is discussed in section VI.C, *supra.*

Swap Entity ↓ / Counterparty →		U.S. Person		Non-U.S. Person			
		Non-Foreign Branch	Foreign Branch	U.S. Branch	Guaranteed Entity	Swap Entity SRS	Other Non-U.S. Person or SRS End User
U.S. Swap Entity	Non-Foreign Branch	Yes	Yes	Yes	Yes	Yes	Yes
	Foreign Branch	Yes[1]	Yes[1] *Sub. Comp. Available*	Yes[1]	Yes[1] *Sub. Comp. Available*	Yes[1] *Sub. Comp. Available*	Yes[1, 2] *Sub. Comp. Available*
Non-U.S. Swap Entity	U.S. Branch	Yes	Yes	Yes	Yes	Yes *Sub. Comp. Available*	Yes *Sub. Comp. Available*
	Guaranteed Entity or SRS	Yes[1]	Yes[1] *Sub. Comp. Available*	Yes[1]	Yes[1] *Sub. Comp. Available*	Yes[1] *Sub. Comp. Available*	Yes[1, 3] *Sub. Comp. Available*
	Other Non-U.S. Person	Yes[1]	Yes[1] *Sub. Comp. Available*	Yes[1]	Yes[1] *Sub. Comp. Available*	Yes[1] *Sub. Comp. Available*	No

[1] The Exchange-Traded Exception is available from certain group B and C requirements for certain anonymous, exchange-traded, and cleared foreign-based swaps between the listed parties.

[2] The Limited Foreign Branch Group B Exception is available from the group B requirements for a foreign branch's foreign-based swaps with a foreign counterparty that is an SRS End User or an Other Non-U.S. Person that is not a swap entity, subject to certain conditions.

[3] The Limited Swap Entity SRS/Guaranteed Entity Group B Exception is available from the group B requirements for the foreign-based swaps of each SRS Swap Entity or Guaranteed Swap Entity with a foreign counterparty that is an SRS End User or an Other Non-U.S. Person that is not a swap entity, subject to certain conditions.

D. Table D—Cross-Border Application of the Group C Requirements in Consideration of Related Exceptions

Table D [572] should be read in conjunction with the text of the Final Rule.

[572] As discussed in section VI.A.3, *supra,* the group C requirements are set forth in §§ 23.400 through 23.451 and 23.700 through 23.704 and relate to certain business conduct standards governing the conduct of SDs and MSPs in dealing with their swap counterparties, and the segregation of assets held as collateral in certain uncleared swaps. Exceptions from the group C requirements are discussed in sections VI.B.2 and VI.B.3, *supra.*

Swap Entity ↓	Counterparty →	U.S. Person		Non-U.S. Person			
		Non-Foreign Branch	Foreign Branch	U.S. Branch	Guaranteed Entity	SRS	Other Non-U.S. Person
U.S. Swap Entity	Non-Foreign Branch	Yes	Yes	Yes	Yes	Yes	Yes
	Foreign Branch	Yes[1]	No	Yes[1]	No	No	No
Non-U.S. Swap Entity	U.S. Branch	Yes	Yes	Yes	Yes	No	No
	Guaranteed Entity or SRS	Yes[1]	No	Yes[1]	No	No	No
	Other Non-U.S. Person	Yes[1]	No	Yes[1]	No	No	No

[1]The Exchange-Traded Exception is available from certain group B and C requirements for certain anonymous, exchange-traded, and cleared foreign-based swaps between the listed parties.

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List of Subjects in 17 CFR Part 23

Business conduct standards, Counterparties, Cross-border, Definitions, De minimis exception, Major swap participants, Swaps, Swap Dealers.

For the reasons stated in the preamble, the Commodity Futures Trading Commission amends 17 CFR part 23 as follows:

PART 23—SWAP DEALERS AND MAJOR SWAP PARTICIPANTS

■ 1. The authority citation for part 23 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 6, 6a, 6b, 6b–1, 6c, 6p, 6r, 6s, 6t, 9, 9a, 12, 12a, 13b, 13c, 16a, 18, 19, 21.

Section 23.160 also issued under 7 U.S.C. 2(i); Sec. 721(b), Public Law 111–203, 124 Stat. 1641 (2010).

■ 2. Add § 23.23 to read as follows:

§ 23.23 Cross-border application.

(a) *Definitions.* Solely for purposes of this section the terms listed in this paragraph (a) have the meanings set forth in paragraphs (a)(1) through (24) of this section. A person may rely on a written representation from its counterparty that the counterparty does or does not satisfy the criteria for one or more of the definitions listed in paragraphs (a)(1) through (24) of this section, unless such person knows or has reason to know that the representation is not accurate; for the purposes of this rule a person would have reason to know the representation is not accurate if a reasonable person should know, under all of the facts of which the person is aware, that it is not accurate.

(1) An *affiliate of,* or a *person affiliated with a specific person,* means a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified.

(2) *Control* including the terms controlling, controlled by, and under common control with, means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting shares, by contract, or otherwise.

(3) *Foreign branch* means any office of a U.S. bank that:

(i) Is located outside the United States;

(ii) Operates for valid business reasons;

(iii) Maintains accounts independently of the home office and of the accounts of other foreign branches, with the profit or loss accrued at each branch determined as a separate item for each foreign branch; and

(iv) Is engaged in the business of banking and is subject to substantive regulation in banking or financing in the jurisdiction where it is located.

(4) *Foreign-based swap* means:

(i) A swap by a non-U.S. swap entity, except for a swap booked in a U.S. branch; or

(ii) A swap conducted through a foreign branch.

(5) *Foreign counterparty* means:

(i) A non-U.S. person, except with respect to a swap booked in a U.S. branch of that non-U.S. person; or

(ii) A foreign branch where it enters into a swap in a manner that satisfies the definition of a swap conducted through a foreign branch.

(6) *Group A requirements* mean the requirements set forth in § 3.3 of this chapter, §§ 23.201, 23.203, 23.600, 23.601, 23.602, 23.603, 23.605, 23.606, 23.607, 23.609 and, to the extent it duplicates § 23.201, § 45.2(a) of this chapter.

(7) *Group B requirements* mean the requirements set forth in §§ 23.202 and 23.501 through 23.504.

(8) *Group C requirements* mean the requirements set forth in §§ 23.400 through 23.451 and 23.700 through 23.704.

(9) *Guarantee* means an arrangement pursuant to which one party to a swap has rights of recourse against a guarantor, with respect to its counterparty's obligations under the swap. For these purposes, a party to a swap has rights of recourse against a guarantor if the party has a conditional or unconditional legally enforceable right to receive or otherwise collect, in whole or in part, payments from the guarantor with respect to its counterparty's obligations under the swap. In addition, in the case of any arrangement pursuant to which the guarantor has a conditional or unconditional legally enforceable right to receive or otherwise collect, in whole or in part, payments from any other guarantor with respect to the counterparty's obligations under the swap, such arrangement will be deemed a guarantee of the counterparty's obligations under the swap by the other guarantor. Notwithstanding the foregoing, until December 31, 2027, a person may continue to classify counterparties based on:

(i) Representations that were made pursuant to the ''guarantee'' definition in § 23.160(a)(2) prior to the effective date of this section; or

(ii) Representations made pursuant to the interpretation of the term ''guarantee'' in the Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 FR 45292 (Jul. 26, 2013), prior to the effective date of this section.

(10) *Non-U.S. person* means any person that is not a U.S. person.

(11) *Non-U.S. swap entity* means a swap entity that is not a U.S. swap entity.

(12) *Parent entity* means any entity in a consolidated group that has one or more subsidiaries in which the entity has a controlling interest, as determined in accordance with U.S. GAAP.

(13) *Significant risk subsidiary* means any non-U.S. significant subsidiary of an ultimate U.S. parent entity where the ultimate U.S. parent entity has more than $50 billion in global consolidated assets, as determined in accordance with U.S. GAAP at the end of the most recently completed fiscal year, but excluding non-U.S. subsidiaries that are:

(i) Subject to consolidated supervision and regulation by the Board of Governors of the Federal Reserve System as a subsidiary of a U.S. bank holding company or an intermediate holding company; or

(ii) Subject to capital standards and oversight by the subsidiary's home country supervisor that are consistent with the Basel Committee on Banking Supervision's ''International Regulatory Framework for Banks'' and subject to margin requirements for uncleared swaps in a jurisdiction that the Commission has found comparable pursuant to a published comparability determination with respect to uncleared swap margin requirements.

(14) *Significant subsidiary* means a subsidiary, including its subsidiaries, which meets any of the following conditions:

(i) The three year rolling average of the subsidiary's equity capital is equal to or greater than five percent of the three year rolling average of the ultimate U.S. parent entity's consolidated equity capital, as determined in accordance with U.S. GAAP as of the end of the most recently completed fiscal year;

(ii) The three year rolling average of the subsidiary's total revenue is equal to or greater than ten percent of the three year rolling average of the ultimate U.S. parent entity's total consolidated revenue, as determined in accordance with U.S. GAAP as of the end of the most recently completed fiscal year; or

(iii) The three year rolling average of the subsidiary's total assets is equal to or greater than ten percent of the three year rolling average of the ultimate U.S. parent entity's total consolidated assets, as determined in accordance with U.S. GAAP as of the end of the most recently completed fiscal year.

(15) *Subsidiary* means an affiliate of a person controlled by such person directly, or indirectly through one or more intermediaries.

(16) *Swap booked in a U.S. branch* means a swap entered into by a U.S. branch where the swap is reflected in the local accounts of the U.S. branch.

(17) *Swap conducted through a foreign branch* means a swap entered into by a foreign branch where:

(i) The foreign branch or another foreign branch is the office through which the U.S. person makes and receives payments and deliveries under the swap pursuant to a master netting or similar trading agreement, and the documentation of the swap specifies that the office for the U.S. person is such foreign branch;

(ii) The swap is entered into by such foreign branch in its normal course of business; and

(iii) The swap is reflected in the local accounts of the foreign branch.

(18) *Swap entity* means a person that is registered with the Commission as a swap dealer or major swap participant pursuant to the Act.

(19) *Ultimate U.S. parent entity* means the U.S. parent entity that is not a subsidiary of any other U.S. parent entity.

(20) *United States and U.S.* means the United States of America, its territories and possessions, any State of the United States, and the District of Columbia.

(21) *U.S. branch* means a branch or agency of a non-U.S. banking organization where such branch or agency:

(i) Is located in the United States;

(ii) Maintains accounts independently of the home office and other U.S. branches, with the profit or loss accrued at each branch determined as a separate item for each U.S. branch; and

(iii) Engages in the business of banking and is subject to substantive banking regulation in the state or district where located.

(22) *U.S. GAAP* means U.S. generally accepted accounting principles.

(23) *U.S. person:*

(i) Except as provided in paragraph (a)(23)(iii) of this section, U.S. person means any person that is:

(A) A natural person resident in the United States;

(B) A partnership, corporation, trust, investment vehicle, or other legal person organized, incorporated, or established under the laws of the United States or having its principal place of business in the United States;

(C) An account (whether discretionary or non-discretionary) of a U.S. person; or

(D) An estate of a decedent who was a resident of the United States at the time of death.

(ii) For purposes of this section, principal place of business means the location from which the officers, partners, or managers of the legal person primarily direct, control, and coordinate the activities of the legal person. With respect to an externally managed investment vehicle, this location is the office from which the manager of the vehicle primarily directs, controls, and coordinates the investment activities of the vehicle.

(iii) The term U.S. person does not include the International Monetary Fund, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, the African Development Bank, the United Nations, and their agencies and pension plans, and any other similar international organizations, and their agencies and pension plans.

(iv) Notwithstanding paragraph (a)(23)(i) of this section, until December 31, 2027, a person may continue to classify counterparties as U.S. persons based on:

(A) Representations made pursuant to the ''U.S. person'' definition in § 23.160(a)(10) prior to the effective date of this section; or

(B) Representations made pursuant to the interpretation of the term ''U.S. person'' in the Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 FR 45292 (Jul. 26, 2013), prior to the effective date of this section.

(24) *U.S. swap entity* means a swap entity that is a U.S. person.

(b) *Cross-border application of swap dealer de minimis registration threshold calculation.* For purposes of determining whether an entity engages in more than a de minimis quantity of swap dealing activity under paragraph (4)(i) of the swap dealer definition in § 1.3 of this chapter, a person shall include the following swaps (subject to paragraph (d) of this section and paragraph (6) of the swap dealer definition in § 1.3 of this chapter):

(1) If such person is a U.S. person or a significant risk subsidiary, all swaps connected with the dealing activity in which such person engages.

(2) If such person is a non-U.S. person (other than a significant risk subsidiary), all of the following swaps connected with the dealing activity in which such person engages:

(i) Swaps with a counterparty that is a U.S. person, other than swaps conducted through a foreign branch of a registered swap dealer.

(ii) Swaps where the obligations of such person under the swaps are subject to a guarantee by a U.S. person.

(iii) Swaps with a counterparty that is a non-U.S. person where the counterparty's obligations under the swaps are subject to a guarantee by a U.S. person, except when:

(A) The counterparty is registered as a swap dealer; or

(B) The counterparty's swaps are subject to a guarantee by a U.S. person that is a non-financial entity; or

(C) The counterparty is itself below the swap dealer de minimis threshold under paragraph (4)(i) of the swap dealer definition in § 1.3, and is affiliated with a registered swap dealer.

(c) *Cross-border application of major swap participant tests.* For purposes of determining a person's status as a major swap participant, as defined in § 1.3 of this chapter, a person shall include the following swap positions (subject to paragraph (d) of this section and the major swap participant definition in § 1.3 of this chapter):

(1) If such person is a U.S. person or a significant risk subsidiary, all swap positions that are entered into by the person.

(2) If such person is a non-U.S. person (other than a significant risk subsidiary), all of the following swap positions of such person:

(i) Swap positions where the counterparty is a U.S. person, other than swaps conducted through a foreign branch of a registered swap dealer.

(ii) Swap positions where the obligations of such person under the swaps are subject to a guarantee by a U.S. person.

(iii) Swap positions with a counterparty that is a non-U.S. person where the counterparty's obligations under the swaps are subject to a guarantee by a U.S. person, except when the counterparty is registered as a swap dealer.

(d) *Exception from counting for certain exchange-traded and cleared swaps.* Notwithstanding any other provision of § 23.23, for purposes of determining whether a non-U.S. person (other than a significant risk subsidiary or a non-U.S. person whose performance under the swap is subject to a guarantee by a U.S. person) engages in more than a de minimis quantity of swap dealing activity under paragraph (4)(i) of the swap dealer definition in § 1.3 of this chapter or for determining the non-U.S. person's status as a major swap participant as defined in § 1.3 of this chapter, such non-U.S. person does not need to count any swaps or swap positions, as applicable, that are entered into by such non-U.S. person on a designated contract market, a registered swap execution facility or a swap execution facility exempted from registration by the Commission pursuant to section 5h(g) of the Act, or a registered foreign board of trade, and cleared through a registered derivatives clearing organization or a clearing organization that has been exempted from registration by the Commission pursuant to section 5b(h) of the Act, where the non-U.S. person does not know the identity of the counterparty to the swap prior to execution.

(e) *Exceptions from certain swap requirements for certain foreign swaps.* (1) With respect to its foreign-based swaps, each non-U.S. swap entity and foreign branch of a U.S. swap entity shall be excepted from:

(i) The group B requirements (other than § 23.202(a) introductory text and (a)(1)) and the group C requirements with respect to any swap—

(A) Entered into on a designated contract market, a registered swap execution facility or a swap execution facility exempted from registration by the Commission pursuant to section 5h(g) of the Act, or a registered foreign board of trade;

(B) Cleared through a registered derivatives clearing organization or a clearing organization that has been exempted from registration by the Commission pursuant to section 5b(h) of the Act; and

(C) Where the swap entity does not know the identity of the counterparty to the swap prior to execution; and

(ii) The group C requirements with respect to any swap with a foreign counterparty.

(2) A non-U.S. swap entity shall be excepted from the group C requirements with respect to any swap booked in a U.S. branch with a foreign counterparty that is neither a foreign branch nor a person whose performance under the swap is subject to a guarantee by a U.S. person.

(3) With respect to its foreign-based swaps, each non-U.S. swap entity that is neither a significant risk subsidiary nor a person whose performance under the swap is subject to a guarantee by a U.S. person shall be excepted from the group B requirements with respect to any swap with a foreign counterparty (other than a foreign branch) that is neither—

(i) A significant risk subsidiary that is a swap entity nor

(ii) A person whose performance under the swap is subject to a guarantee by a U.S. person.

(4) With respect to its foreign-based swaps, each foreign branch of a U.S. swap entity shall be excepted from the group B requirements with respect to any swap with a foreign counterparty (other than a foreign branch) that is neither a swap entity nor a person whose performance under the swap is subject to a guarantee by a U.S. person, subject to the following conditions:

(i) A group B requirement is not eligible for the exception if the requirement, as applicable to the swap, is eligible for substituted compliance pursuant to a comparability determination issued by the Commission prior to the execution of the swap; and

(ii) In any calendar quarter, the aggregate gross notional amount of swaps conducted by a swap entity in reliance on this exception does not exceed five percent (5%) of the aggregate gross notional amount of all its swaps.

(5) With respect to its foreign-based swaps, each non-U.S. swap entity that is a significant risk subsidiary (an ''SRS

SE'') or a person whose performance under the swap is subject to a guarantee by a U.S. person (a ''Guaranteed SE'') shall be excepted from the group B requirements with respect to any swap with a foreign counterparty (other than a foreign branch) that is neither a swap entity nor a person whose performance under the swap is subject to a guarantee by a U.S. person, subject to the following conditions:

(i) A group B requirement is not eligible for the exception if the requirement, as applicable to the swap, is eligible for substituted compliance pursuant to a comparability determination issued by the Commission prior to the execution of the swap; and

(ii) In any calendar quarter, the aggregate gross notional amount of swaps conducted by an SRS SE or a Guaranteed SE in reliance on this exception aggregated with the gross notional amount of swaps conducted by all affiliated SRS SEs and Guaranteed SEs in reliance on this exception does not exceed five percent (5%) of the aggregate gross notional amount of all swaps entered into by the SRS SE or Guaranteed SE and all affiliated swap entities.

(f) *Substituted Compliance.* (1) A non-U.S. swap entity may satisfy any applicable group A requirement by complying with the applicable standards of a foreign jurisdiction to the extent permitted by, and subject to any conditions specified in, a comparability determination issued by the Commission under paragraph (g) of this section;

(2) With respect to its foreign-based swaps, a non-U.S. swap entity or foreign branch of a U.S. swap entity may satisfy any applicable group B requirement for a swap with a foreign counterparty by complying with the applicable standards of a foreign jurisdiction to the extent permitted by, and subject to any conditions specified in, a comparability determination issued by the Commission under paragraph (g) of this section; and

(3) A non-U.S. swap entity may satisfy any applicable group B requirement for any swap booked in a U.S. branch with a foreign counterparty that is neither a foreign branch nor a person whose performance under the swap is subject to a guarantee by a U.S. person by complying with the applicable standards of a foreign jurisdiction to the extent permitted by, and subject to any conditions specified in, a comparability determination issued by the Commission under paragraph (g) of this section.

(g) *Comparability determinations.* (1) The Commission may issue comparability determinations under this section on its own initiative.

(2) *Eligibility requirements.* The following persons may, either individually or collectively, request a comparability determination with respect to some or all of the group A requirements and group B requirements:

(i) A swap entity that is eligible, in whole or in part, for substituted compliance under this section or a trade association or other similar group on behalf of its members who are such swap entities; or

(ii) A foreign regulatory authority that has direct supervisory authority over one or more swap entities subject to the group A requirements and/or group B requirements and that is responsible for administering the relevant foreign jurisdiction's swap standards.

(3) *Submission requirements.* Persons requesting a comparability determination pursuant to this section shall electronically provide the Commission:

(i) A description of the objectives of the relevant foreign jurisdiction's standards and the products and entities subject to such standards;

(ii) A description of how the relevant foreign jurisdiction's standards address, at minimum, the elements or goals of the Commission's corresponding requirements or group of requirements. Such description should identify the specific legal and regulatory provisions that correspond to each element or goal and, if necessary, whether the relevant foreign jurisdiction's standards do not address a particular element or goal;

(iii) A description of the differences between the relevant foreign jurisdiction's standards and the Commission's corresponding requirements, and an explanation regarding how such differing approaches achieve comparable outcomes;

(iv) A description of the ability of the relevant foreign regulatory authority or authorities to supervise and enforce compliance with the relevant foreign jurisdiction's standards. Such description should discuss the powers of the foreign regulatory authority or authorities to supervise, investigate, and discipline entities for compliance with the standards and the ongoing efforts of the regulatory authority or authorities to detect and deter violations of, and ensure compliance with, the standards;

(v) Copies of the foreign jurisdiction's relevant standards (including an English translation of any foreign language document); and

(vi) Any other information and documentation that the Commission deems appropriate.

(4) *Standard of review.* The Commission may issue a comparability determination pursuant to this section to the extent that it determines that some or all of the relevant foreign jurisdiction's standards are comparable to the Commission's corresponding requirements or group of requirements, or would result in comparable outcomes as the Commission's corresponding requirements or group of requirements, after taking into account such factors as the Commission determines are appropriate, which may include:

(i) The scope and objectives of the relevant foreign jurisdiction's standards;

(ii) Whether the relevant foreign jurisdiction's standards achieve comparable outcomes to the Commission's corresponding requirements;

(iii) The ability of the relevant regulatory authority or authorities to supervise and enforce compliance with the relevant foreign jurisdiction's standards; and

(iv) Whether the relevant regulatory authority or authorities has entered into a memorandum of understanding or other arrangement with the Commission addressing information sharing, oversight, examination, and supervision of swap entities relying on such comparability determination.

(5) *Reliance.* Any swap entity that, in accordance with a comparability determination issued under this section, complies with a foreign jurisdiction's standards, would be deemed to be in compliance with the Commission's corresponding requirements. Accordingly, if a swap entity has failed to comply with the foreign jurisdiction's standards or a comparability determination, the Commission may initiate an action for a violation of the Commission's corresponding requirements. All swap entities, regardless of whether they rely on a comparability determination, remain subject to the Commission's examination and enforcement authority.

(6) *Discretion and Conditions.* The Commission may issue or decline to issue comparability determinations under this section in its sole discretion. In issuing such a comparability determination, the Commission may impose any terms and conditions it deems appropriate.

(7) *Modifications.* The Commission reserves the right to further condition, modify, suspend, terminate, or otherwise restrict a comparability determination issued under this section in the Commission's discretion.

(8) *Delegation of authority.* The Commission hereby delegates to the Director of the Division of Swap Dealer and Intermediary Oversight, or such other employee or employees as the Director may designate from time to time, the authority to request information and/or documentation in connection with the Commission's issuance of a comparability determination under this section.

(h) *Records, scope of application, effective and compliance dates*—(1) *Records.* Swap dealers and major swap participants shall create a record of their compliance with this section and shall retain records in accordance with § 23.203.

(2) *Scope of Application.* The requirements of this section shall not apply to swaps executed prior to September 14, 2021.

(3) *Effective date and compliance date.* (i) This section shall be effective on the date that is 60 days following its publication in the **Federal Register**.

(ii) Provided that swap dealers and major swap participants comply with the recordkeeping requirements in paragraph (h)(1) of this section, the exceptions in paragraph (e) of this section are effective upon the effective date of the rule.

(iii) Swap dealers and major swap participants must comply with the requirements of this section no later than September 14, 2021.

Issued in Washington, DC, on July 24, 2020, by the Commission.

Christopher Kirkpatrick,

Secretary of the Commission.

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

Appendices to Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants—Commission Voting Summary, Chairman's Statement, and Commissioners' Statements

Appendix 1—Commission Voting Summary

On this matter, Chairman Tarbert and Commissioners Quintenz and Stump voted in the affirmative. Commissioners Behnam and Berkovitz voted in the negative.

Appendix 2—Supporting Statement of Chairman Heath P. Tarbert

President John Adams once warned: ''Great is the guilt of unnecessary war.'' [1] While he was obviously referring to military conflicts, his admonition applies to conflicts among nations more generally. Financial regulation has not been exempt from international discord. And in recent years, the CFTC's own cross-border guidance on swaps has caused concerns about a regulatory arms race and the balkanization of global financial markets. Consider the following entreaties by our overseas allies and regulatory counterparts:

''*At a time of highly fragile economic growth, we believe that it is critical to avoid taking steps that risk withdrawal from global financial markets into inevitably less efficient regional or national markets.*''

—Letter from the Finance Ministers of the United Kingdom, France, Japan, and the European Commission to CFTC Chairman regarding the CFTC's cross-border guidance (Oct. 17, 2012)

''*We believe a failure to address [our] concerns could have unintended consequences, including increasing market fragmentation and, potentially, systemic risk in these markets, as well as unduly increasing the compliance burden on industry and regulators.*''

—Letter from the Australian Securities and Investments Commission, the Hong Kong Monetary Authority, the Monetary Authority of Singapore, the Reserve Bank of Australia, and the Securities and Futures Commission of Hong Kong to CFTC Chairman regarding the CFTC's cross-border guidance (Aug. 27, 2012)

''*. . . [U]sing personnel or agents located in the U.S. would not be a sufficient criterion supporting the duplication of applicable sets of rules to transactions [between non-U.S. persons,] and [we] ask you to consider not directly applying rules on this basis.*''

—Letter from Steven Maijoor, Chair, European Securities and Markets Authority to Acting CFTC Chairman regarding the CFTC staff's ''ANE Advisory,'' No. 13–69 (Mar. 13, 2014)

I will leave it to others to debate whether the international discord caused by the CFTC's cross-border guidance [2] and related staff advisory [3] was ''necessary'' at the time it was introduced. Far more constructive is for us to ask whether it is necessary today. For me, there is but one conclusion: Because nearly all G20 jurisdictions have adopted similar swaps regulations pursuant to the Pittsburgh Accords,[4] it is unnecessary for the CFTC to be the world's policeman for all swaps.

On this basis, I am pleased to support the Commission's final rule on the cross-border application of registration thresholds and certain requirements for swap dealers and major swap participants (''swap entities''). This final rule provides critically needed regulatory certainty to the global swaps markets. And I believe it properly balances protection of our national interests with appropriate deference to international counterparts.

Need for Rule-Based Finality

As noted above, the Commission's 2013 Guidance left much to be desired by both our market participants and our regulatory colleagues overseas. The action was taken outside the standard rulemaking process under the Administrative Procedure Act,[5] so was merely ''guidance'' that is not technically enforceable. But because market participants as a practical matter followed it nonetheless, it had a sweeping impact on the global swaps markets. Over the intervening years, a patchwork of staff advisories and no-action letters has supplemented the 2013 Guidance. With almost seven years of experience, it is high time for the Commission to bring finality to the issues the 2013 Guidance and its progeny sought to address.

Congressional Mandate

We call this final rule a ''cross-border'' rule, and in certain respects it is. For example, the rule addresses when non-U.S. persons must count dealing swaps with U.S. persons, including foreign branches of American banks, toward the *de minimis* threshold in our swap dealer definition. More fundamentally, however, the rule answers a basic question: *What swap dealing activity outside the United States should trigger CFTC registration and other requirements?*

To answer this question, we must turn to section 2(i) of the Commodity Exchange Act (''CEA''),[6] a provision Congress added in Title VII of the Dodd-Frank Act. Section 2(i) provides that the CEA does not apply to swaps activities outside the United States except in two circumstances: (1) Where activities have a ''direct and significant connection with activities in, or effect on, commerce of the United States'' or (2) where they run afoul of the Commission's rules or regulations that prevent evasion of Title VII. Section 2(i) evidences Congress's clear intent for the U.S. swaps regulatory regime to stop at the water's edge, except where foreign activities either are closely and meaningfully related to U.S. markets or are vehicles to evade our laws and regulations.

I believe the final rule we issue today is a levelheaded approach to the exterritorial application of our swap dealer registration regime and related requirements, and it fully implements the congressional mandate in section 2(i). At the same time, it acknowledges the important role played by the CFTC's domestic and international counterparts in regulating parts of the global swaps markets. In short, the final rule employs neither a full-throated ''intergalactic commerce clause'' [7] nor an isolationist

[1] Letter from John Adams to Abigail Adams, 19 May 1794 [electronic edition]. *Adams Family Papers: An Electronic Archive,* Massachusetts Historical Society, *http://www.masshist.org/digitaladams/.*

[2] Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 FR 45292 (July 26, 2013) (''2013 Guidance''), *http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2013-17958a.pdf.*

[3] CFTC Staff Advisory No. 13–69 (Nov. 14, 2013), *https://www.cftc.gov/node/212831.*

[4] Financial Stability Board, *Annual Report on Implementation and Effects of the G20 Financial Regulatory Reforms* 3 (Oct. 16, 2019) (showing that a very large majority of FSB jurisdictions have implemented the G20 priority reforms for over-the-counter derivatives).

[5] 5 U.S.C. 551 *et seq.*

[6] 7 U.S.C. 2(i).

[7] Commissioner Jill E. Sommers, Statement of Concurrence: (1) Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, Proposed Interpretive Guidance and

Continued

mentality. It is thoughtful and balanced, and it will avoid future unnecessary conflicts among regulators.

Guiding Principles for Regulating Foreign Activities

As I have stated before,[8] I am guided by three additional principles in considering the extent to which the CFTC should make use of our extraterritorial powers.

1. Protect the National Interest

An important role of the CFTC is to protect and advance the interests of the United States. In this regard, Congress provided the CFTC with explicit extraterritorial power to safeguard the U.S. financial system where swaps activities are concerned.

It is incumbent upon us to guard against risks created outside the United States flowing back into our country. But our focus cannot be on *all* risks. Congress made that clear in section 2(i). It would be a markedly poor use of American taxpayers' dollars to regulate swaps activities in far-flung lands simply to prevent every risk that might have a nexus to the United States. It would also divert the CFTC from channeling our resources where they matter the most: To our own markets and participants. The rule therefore focuses on instances where material risks from abroad are most likely to come back to the United States and where no one but the CFTC is responsible for those risks.

Hence, guarantees of offshore swaps by U.S. parent companies are counted toward our registration requirements because that risk is effectively underwritten and borne in the United States. The same is true with the concept of a ''significant risk subsidiary'' (''SRS''). As explained in the rule, an SRS is a large non-U.S. subsidiary of a large U.S. company that deals in swaps outside the United States but (1) is not subject to comparable capital and margin requirements in its home country, and (2) is not a subsidiary of a holding company subject to consolidated supervision by an American regulator, namely the Federal Reserve Board. Our final cross-border rule requires an SRS to register as a swap dealer or major swap participant with the CFTC if the SRS exceeds the same registration thresholds as a U.S. firm operating within the United States. The national interest demands it.[9]

2. Follow Kant's Categorical Imperative

As I said when we proposed this rule, I believe cross-border rulemaking should follow Kant's ''categorical imperative'': We should act according to the maxim that we wish all other rational people to follow, as if it were a universal law.[10]

What I take from that is that we should ourselves establish a regulatory regime that we believe should be the global convention. How would this work? Let me start by explaining how it would not work. If we impose our regulations on non-U.S. persons whenever they have a remote nexus to the United States, then we should be willing for all other jurisdictions to do the same. The end result would be absurdity, with everyone trying to regulate everyone else. And the duplicative and overlapping regulations would inevitably lead to fragmentation in the global swaps markets—itself a potential source of systemic risk.[11] Instead, we should adopt a framework that applies CFTC regulations outside the United States only when it addresses one or more important risks to our markets.

Furthermore, we should afford comity to other regulators who have adopted comparable regulations, just as we expect them to do for us. This is especially important when we evaluate whether foreign subsidiaries of U.S. parent companies could pose a significant risk to our financial system. The categorical imperative leads us to an unavoidable result: We should not impose our regulations on the non-U.S. activities of non-U.S. companies in those jurisdictions that have comparable capital and margin requirements to our own.[12] By the same token, when U.S. subsidiaries of foreign companies operate within our borders, we expect them to follow our laws and regulations and not simply comply with rules from their home country.

Charity, it is often said, begins at home. The categorical imperative further compels us to avoid duplicating the work of other American regulators. If a foreign subsidiary of a U.S. financial institution is subject to consolidated regulation and supervision by the Federal Reserve Board, then we should defer to our domestic counterparts on questions of dealing activity outside the United States. The Federal Reserve Board has extensive regulatory and supervisory tools to ensure a holding company is prudent in its risk-taking at home and abroad.[13] The CFTC instead should focus on regulating dealing activity within the United States or with U.S. persons.

3. Pursue SEC Harmonization Where Appropriate

As I said in connection with our proposal of this rule, I find it surreal that the SEC and the CFTC, two federal agencies that regulate similar products pursuant to the same title of the same statute—with an explicit mandate to ''consult and coordinate'' with each other—have not agreed until today on how to define ''U.S. person.'' This failure to coordinate has unnecessarily increased operational and compliance costs for market participants.[14] I am pleased that this final rule uses the same definition of ''U.S. person'' as the SEC's cross-border rulemaking.

To be sure, as my colleagues have said on several occasions, we should not harmonize with the SEC merely for the sake of harmonization.[15] We should do so only if it

Policy Statement; (2) Notice of Proposed Exemptive Order and Request for Comment Regarding Compliance with Certain Swap Regulations (June 29, 2012), *https://www.cftc.gov/PressRoom/SpeechesTestimony/sommersstatement062912* (noting that ''staff had been guided by what could only be called the 'Intergalactic Commerce Clause' of the United States Constitution, in that every single swap a U.S. person enters into, no matter what the swap or where it was transacted, was stated to have a direct and significant connection with activities in, or effect on, commerce of the United States'').

[8] Statement of Chairman Heath P. Tarbert in Support of the Cross-Border Swaps Proposal (Dec. 18, 2019), *https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement121819.*

[9] The SRS concept is designed to address a potential situation where a U.S. entity establishes an offshore subsidiary to conduct its swap dealing business without an explicit guarantee on the swaps in order to avoid U.S. regulation. For example, the U.S.-regulated insurance company American International Group (''AIG'') nearly failed as a result of risk incurred by the London swap trading operations of its subsidiary AIG Financial Products. *See, e.g.,* Congressional Oversight Panel, June Oversight Report, *The AIG Rescue, Its Impact on Markets, and the Government's Exit Strategy* (June 10, 2010), *http://www.gpo.gov/fdsys/pkg/CPRT-111JPRT56698/pdf/CPRT-111JPRT56698.pdf.* If the Commission did not regulate SRSs, an AIG-type entity could establish a non-U.S. affiliate to conduct its swaps dealing business, and, so long as it did not explicitly guarantee the swaps, it would avoid application of the Dodd-Frank Act and bring risk created offshore back into the United States without appropriate regulatory safeguards.

[10] ''Act only according to that maxim whereby you can, at the same time, will that it should become a universal law.'' Immanuel Kant, *Grounding for the Metaphysics of Morals* (1785) [1993], translated by James W. Ellington (3rd ed.).

[11] *See* Financial Stability Board, *Annual Report on Implementation and Effects of the G20 Financial Regulatory Reforms* 3 (Oct. 16, 2019).

[12] *See, e.g.,* Comments of the European Commission in respect of CFTC Staff Advisory No. 13–69 regarding the applicability of certain CFTC regulations to the activity in the United States of swap dealers and major swap participants established in jurisdictions other than the United States (Mar. 10, 2014), *https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=59781&SearchText=* (''In order to ensure that cross-border activity is not inhibited by the application of inconsistent, conflicting or duplicative rules, regulators must work together to provide for the application of one set of comparable rules, where our rules achieve the same outcomes. Rules should therefore include the possibility to defer to those of the host regulator in most cases.''); FSB Fragmentation Report, *supra* note 11, at 8 (noting that the G20 ''has agreed that jurisdictions and regulators should be able to defer to each other when it is justified by the quality of their respective regulatory and enforcement regimes, based on similar outcomes in a non-discriminatory way, paying due respect to home country regulation regimes'').

[13] For example, the Federal Reserve Board requires all foreign branches and subsidiaries ''to ensure that their operations conform to high standards of banking and financial prudence.'' 12 CFR 211.13(a)(1). Furthermore, they are subject to examinations on compliance. *See Bank Holding Company Supervision Manual,* Section 3550.0.9 (''The procedures involved in examining foreign subsidiaries of domestic bank holding companies are generally the same as those used in examining domestic subsidiaries engaged in similar activities.'').

[14] *See, e.g.,* Futures Industry Association Letter re: Harmonization of SEC and CFTC Regulatory Frameworks (Nov. 29, 2018), *https://fia.org/articles/fia-offers-recommendations-cftc-and-sec-harmonization.*

[15] *See, e.g.,* Dissenting Statement of Commissioner Dan M. Berkovitz, Rulemaking to Provide Exemptive Relief for Family Office CPOs: Customer Protection Should be More Important than Relief for Billionaires (Nov. 25, 2019), *https://www.cftc.gov/PressRoom/SpeechesTestimony/berkovitzstatement112519* (''The Commission eliminates the notice requirement largely on the basis that this will harmonize the Commission's regulations with those of the SEC. Harmonization for harmonization's sake is not a rational basis for agency action.'').

is sensible. In the first instance, we must determine whether Congress has explicitly asked us to do something different or implicitly did so by giving us a different statutory mandate. We must also consider whether differences in our respective products or markets warrant a divergent approach. Just as today's final rule takes steps toward harmonization, it also diverges where appropriate.

The approach we have taken with respect to ''ANE Transactions'' is deliberately different than the SEC's.[16] ANE Transactions are swap (or security-based swap) transactions between two non-U.S. persons that are ''arranged, negotiated, or executed'' by their personnel or agents located in the United States, but booked to entities outside America. While some or all of the front-end sales activity takes place in the United States, the financial risk of the transactions resides overseas.

Here, key differences in the markets for swaps and security-based swaps are dispositive. The swaps market is far more global than the security-based swaps market. While commodities such as gold and oil are traded throughout the world, equity and debt securities trade predominantly in the jurisdictions where they were issued. For this reason, security-based swaps are inextricably tied to the underlying security, and vice versa. This is particularly the case with single-name credit default swaps, where the arranging, negotiating, or execution is typically done in the United States because the underlying reference entity is a U.S. company. More generally, security-based swaps can affect the price and liquidity of the underlying security, so the SEC has a legitimate interest in regulating transactions in those instruments. By contrast, because commodities are traded globally, there is less need for the CFTC to apply its swaps rules to ANE Transactions.[17]

Moreover, as noted above, Congress directed the CFTC to regulate foreign swaps activities outside the United States that have a ''direct and significant'' connection to our financial system. Congress did not give a similar mandate to the SEC. As a result, the SEC has not crafted its cross-border rule to extend to an SRS engaged in security-based swap dealing activity offshore that may pose a systemic risk to our financial system. Our rule does with respect to swaps, aiming to protect American taxpayers from another Enron conducting its swaps activities through a major foreign subsidiary without CFTC oversight.

The final rule addresses Transaction-Level Requirements applicable to swap entities (specifically, the Group B and Group C requirements), but does not cover other Transaction-Level Requirements, such as the reporting, clearing, and trade execution requirements. The Commission intends to address these remaining Transaction-Level Requirements (the ''Unaddressed TLRs'') in connection with future cross-border rulemakings. Until such time, the Commission will not consider, as a matter of policy, a non-U.S. swap entity's use of their personnel or agents located in the United States to ''arrange, negotiate, or execute'' swap transactions with non-U.S. counterparties for purposes of determining whether Unaddressed TLRs apply to such transactions.

In connection with the final rule, DSIO has withdrawn Staff Advisory No. 13–69,[18] and, together with the Division of Clearing and Risk and the Division of Market Oversight, granted certain non-U.S. swap dealers no-action relief with respect to the applicability of the Unaddressed TLRs to their transactions with non-U.S. counterparties that are arranged, negotiated, or executed in the United States. In Staff Advisory 13–69, the CFTC's staff applied Transaction-Level Requirements to ANE Transactions, without the Commission engaging in notice and comment rulemaking to determine whether such an application is appropriate. Going forward, I fully expect that the Commission will first conduct fact-finding to determine the extent to which ANE Transactions raise policy concerns that are not otherwise addressed by the CEA or our regulations.

Refinements to the Proposed Rule

In response to public comment, and consistent with the guiding principles described above, the final rule includes a number of refinements from the proposal issued last December. I will leave it to our extremely knowledgeable staff to outline all the changes in detail, but I will highlight some of the key refinements here. These principally concern the treatment of SRSs and U.S. branches of foreign swap entities.

1. Significant Risk Subsidiaries

As noted, the SRS concept is not intended to reach subsidiaries of holding companies that are subject to consolidated supervision by the Federal Reserve Board. The final rule recognizes that intermediate holding companies of foreign banking organizations under the Federal Reserve Board's Regulation YY are subject to such consolidated supervision, and to enhanced capital, liquidity, risk-management, and stress-testing requirements. Accordingly, foreign subsidiaries of intermediate holding companies are excluded from the SRS definition under the final rule.

In addition, the final rule recognizes that certain SRSs may act as ''customers'' or ''end users'' in the global swaps markets, engaging in only a *de minimis* level of swap dealing or no dealing activity at all. Consistent with the principle of focusing on risk to the United States, the ''Group B'' category of risk-mitigating regulatory requirements will not apply to swaps between a non-U.S. swap entity and an SRS that is simply an end user.[19] This approach will help preserve end users' access to liquidity in foreign markets.

For similar reasons, the final rule also provides a limited exception from the Group B requirements for a swap entity that is an SRS or a guaranteed entity—to the extent that swap entity's counterparty is an SRS end user or an Other Non-U.S. Person that is not a swap entity. In addition, the final rule clarifies that a non-U.S. person that is not itself an SRS or a guaranteed entity need not count swaps with an SRS toward its swap dealer *de minimis* threshold, unless that SRS is a guaranteed entity.

I believe these adjustments to the proposed SRS regime will further serve to channel our regulatory resources, while offering appropriate deference to our domestic and foreign regulatory counterparts.

2. U.S. Branches

The final rule also includes two key changes to the treatment of U.S. branches of foreign swap entities. First, it expands the availability of substituted compliance for the Group B requirements to include swaps between such a U.S. branch, on the one hand, and an SRS or Other Non-U.S. Person, on the other.[20] And second, it creates a new exception from the ''Group C'' external business conduct standards for swaps between U.S. branches and foreign counterparties (other than guaranteed entities and foreign branches of U.S. swap entities). These changes recognize that U.S. branches, though located on U.S. soil, are part of a non-U.S. legal entity. Accordingly, while such branches should be subject to certain risk-mitigating regulations, they should not be subject to the full panoply of requirements applicable to true U.S. persons.

Conclusion

In sum, the final rule before us today provides a critical measure of regulatory certainty for the global swaps markets. I believe the rule is also a sensible and principled approach to addressing when foreign transactions should fall within the CFTC's swap entity registration and related requirements.

I have noted before President Eisenhower's observation that ''The world must learn to

[16] *See* Securities and Exchange Commission, Final Rules and Guidance on Cross-Border Application of Certain Security-Based Swap Requirements, 85 FR 6270, 6272 (Feb. 4, 2020) (stating that ''the [SEC] continues to believe the 'arranged, negotiated, or executed' criteria form an appropriate basis for applying Title VII requirements in the cross-border context'').

[17] Under the final rule, persons engaging in any aspect of swap transactions within the United States remain subject to the CEA provisions and Commission regulations prohibiting the employment, or attempted employment, of manipulative, fraudulent, or deceptive devices, such as section 6(c)(1) of the CEA (7 U.S.C. 9(1)) and Commission regulation 180.1 (17 CFR 180.1). The Commission thus would retain anti-fraud and anti-manipulation authority, and would continue to monitor the trading practices of non-U.S. persons that occur within the territory of the United States in order to enforce a high standard of customer protection and market integrity. Even where a swap is entered into by two non-U.S. persons, we have a significant interest in deterring fraudulent or manipulative conduct occurring within our borders, and we cannot let our country be a haven for such activity.

[18] CFTC Staff Advisory No. 13–69 (Nov. 14, 2013), *https://www.cftc.gov/sites/default/files/idc/groups/public/@lrlettergeneral/documents/letter/13-69.pdf.*

[19] This exception applies only to ''Other Non-U.S. Person'' swap entities, *i.e.,* non-U.S. swap entities that are neither an SRS nor an entity subject to a U.S. person guarantee (''guaranteed entity''). A non-U.S. swap entity that is an SRS or guaranteed entity would need to rely on the limited Group B exception discussed below.

[20] This expansion of substituted compliance does not apply to swaps between two U.S. branches of non-U.S. swap entities.

work together, or finally it will not work at all.'' I sincerely hope our domestic and international counterparts will view today's action as a positive step toward further cooperation to provide sound regulation to the global swaps markets.

Appendix 3—Supporting Statement of Commissioner Brian Quintenz

I am very pleased to support today's final rule interpreting Congress' statutory directive that the Commission may only regulate those foreign activities that ''have a direct and significant connection with activities in, or effect on commerce, of the United States.'' [1] As I noted when I supported the proposal last December, Congress deliberately placed a clear and strong limitation on the CFTC's extraterritorial reach, recognizing the need for international comity and deference in a global swaps market.[2] Today's rule provides important safeguards to the US financial markets in delineating which cross-border swap activity must be counted towards potential registration with the Commission, and which transactions should be subject to the CFTC's business conduct requirements for swap dealers (SDs) and major swap participants (MSPs). At the same time, the final rule appropriately defers to foreign regulatory regimes to avoid duplicative regulation and disadvantaging U.S. institutions acting in foreign markets.

Today's rule achieves the goals for cross-border regulation that I articulated in a speech before the ISDA Annual Japan Conference in October of last year.[3] I stated that each jurisdiction's recognition of, and deference to, the sovereignty of other jurisdictions is crucial in avoiding market fragmentation that poses serious risks to the liquidity and health of the derivatives markets. This rule properly grants deference to other jurisdictions by limiting the extent to which non-US counterparties must comply with significant aspects of the CFTC's regulatory framework for SDs and MSPs and by providing market participants with the opportunity to comply with local laws that the Commission has deemed comparable to the CFTC's regulations (''substituted compliance'').

Substituted Compliance

As I noted with respect to the proposal, substituted compliance is the lynchpin of a global swaps market, and the absence of regulatory deference has been the fracturing sound we hear when the global swaps market fragments. The final rule provides a framework for substituted compliance with respect to two sets of regulations, ''group A'' entity-level requirements, such as conflicts of interest policies and a risk management program, and ''group B'' transaction-level requirements, such as daily trading records, confirmation, and portfolio reconciliation. While the Commission has issued substituted compliance determinations for entity-level requirements in six jurisdictions and for transaction-level requirements in two jurisdictions, they all contain exceptions for particular provisions of the Commission's regulations, and one of the transaction-level determinations partially addresses only two of the five regulations in group B.[4]

Today's rule provides for a flexible, outcomes-based framework for future comparability determinations that will assess the goals of the Commission's regulations against the standards of its foreign counterparts' regimes, instead of directing the Commission to focus on a rigid line-by-line or even regulation-by-regulation comparison.[5] More specifically, and a primary reason for my support of this final rule, under this new framework, the Commission can compare the goals of its regulations to the outcomes of foreign regulations on an entire group-wide basis, so that the standards of a foreign regime will be considered holistically compared to the goals of all the Commission's either group A or group B requirements.

Additionally, this final rule allows the Commission to proactively assess and issue comparability determinations without waiting for a request from a jurisdiction. I recognize that several G–20 jurisdictions have made significant progress in the area of issuing transaction-level requirements, as evidenced by a recent report by the Financial Stability Board (FSB).[6] I hope that the Commission will soon issue additional substituted compliance determinations in order that foreign firms registered as SDs with the Commission, as well as foreign branches of US SDs, can gain the efficiencies of complying with local laws for many of their transactions with non-US persons.[7] Ideally, future determinations will provide for comprehensive, holistic substituted compliance in a particular jurisdiction for all transaction-level requirements in the CFTC's group B.

ANE

Today's rule properly eliminates the possibility that a non-US SD be required to follow many of the CFTC's transaction-level requirements for a swap opposite a non-US counterparty if US-based personnel of that SD ''arrange, negotiate, or execute'' (ANE) the swap. This action brings to a close almost seven years of uncertainty, beginning with the misguided DSIO Advisory of November 2013.[8] I note that the staff's no-action letter issued this week suspends enforcement of ANE with respect to transaction-level requirements not covered by today's rule, specifically in the areas of real-time reporting of swaps to data repositories and the clearing and trade execution requirements, pending future Commission rulemakings that address these rules in a cross-border context. I expect the Commission will issue such rules in the near future in order to provide the marketplace with legal certainty in these areas and formally dispense with the ANE construct, just as it has with respect to the requirements addressed today. I believe strongly that ANE has no place with respect to real-time reporting, the clearing requirement, or the trade execution requirement, just like it has no place with respect to the business conduct regulations.

US Guarantees and SRS

Another important element of today's rule is that it only requires two, clearly defined classes of non-US entities to count all of their swaps towards the Commission's SD and MSP registration thresholds, and to generally comply with the Commission's SD and MSP rules if registered. The first is an entity whose obligations to a swap are guaranteed by a US person, under a standard consistent with the Commission's cross-border rule for uncleared swap margin requirements.[9] The second is an entity deemed a ''significant risk subsidiary'' (SRS) of a US firm. It is very important that subsidiaries of US bank holding companies, including intermediate subsidiaries, are carved out from the SRS definition. Those firms are subject to supervision by the Federal Reserve Board, and, therefore, it does not make sense for the CFTC to deploy its precious resources to regulating those entities.

Helping US SDs' Foreign Branches Compete

Today's rule properly makes substituted compliance available for group B requirements to a foreign branch of a US SD similarly to how substituted compliance is available for many non-US SDs registered with the Commission. I expect that this will help these branches compete with local institutions in that they will be subject to the same rules. For example, the Commission has already granted substituted compliance to EU regulations with respect to certain group B regulations.[10] As a result, both the EU branch of a US firm registered with the Commission as an SD and an EU firm registered as an SD could comply with many of the same EU rules for swaps with a US person or with a non-US person that is either US-guaranteed or an SRS registered as an SD or MSP (''swap entity SRS''). Moreover, under the ''limited foreign branch group B exception,'' the foreign branch of a US firm would be excused from complying with any group B rules, subject to a 5% notional cap, for a swap with a non-US person that is neither US guaranteed nor a swap entity SRS. However, if substituted compliance has been provided in a jurisdiction, then instead of

[1] Sec. 2(i) of the Commodity Exchange Act.

[2] Supporting Statement of Commissioner Brian Quintenz Regarding Proposed Rule: Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to SDs and MSPs, *https://www.cftc.gov/PressRoom/SpeechesTestimony/quintenzstatement121819b.*

[3] Remarks of CFTC Commissioner Brian Quintenz at 2019 ISDA Annual Japan Conference, ''Significant's Significance,'' *https://www.cftc.gov/PressRoom/SpeechesTestimony/opaquintenz20.*

[4] The determinations are available at, *https://www.cftc.gov/LawRegulation/DoddFrankAct/CDSCP/index.htm.* The transaction-level determination partially addressing only two of the group B regulations is for Japan, 78 FR 78890 (Dec. 27, 2013).

[5] Regulation 23.23(g).

[6] FSB, OTC Derivatives Market Reforms: 2019 Progress Report on Implementation (Oct. 15, 2019), Table M, *https://www.fsb.org/wp-content/uploads/P151019.pdf.*

[7] The availability of substituted compliance, depending on the status of the counterparty, is provided for in regulation 23.23(f)(1) with respect to group A regulations and in 23.23(f)(2) through (3) with respect to group B regulations.

[8] CFTC Staff Advisory 13–69 (Nov. 14, 2013).

[9] Regulation 23.160.

[10] 78 FR 78878 (Dec. 27, 2013).

being excused from the group B rules for those swaps, the foreign branch would have to comply with the local rules. Due to the fact that neither of the transaction-level determinations granted comparability for all of the group B requirements, with respect to those requirements not subject to a substituted compliance determination, the foreign branch may either comply with CFTC regulations or count the notional value of the swap towards its 5% limited group B exception. Clearly, the rules favor the possibility of substituted compliance, pursuant to which a foreign branch of a US firm would have no limitation in following local rules. I believe that group-wide comparability determinations, without any exceptions, would simplify this situation and make more consistent the treatment of US dealer's foreign branches and their local competitors.

In conclusion, I am very pleased to have been a part of the Commission that accomplished this major milestone in a long road of issuing final regulations in the area of cross-border swaps oversight. I would like to thank the staff of the Division of Swap Dealer and Intermediary Oversight for all of their work in completing this final rule and to Chairman Tarbert for his leadership on this important issue.

Appendix 4—Dissenting Statement of Commissioner Rostin Behnam Introduction and Overview

Today, by approving a final rule addressing the cross-border application of the registration thresholds and certain requirements applicable to swap dealers (''SDs'') and major swap participants (''MSPs'') (the ''Final Rule''), the Commodity Futures Trading Commission (''CFTC'' or ''Commission'') overlooks Dodd-Frank Act [1] purposes, Congressional mandates thereunder, an opinion of the DC District Court,[2] and multiple comments raising significant concerns. The Commission instead relies on broad deference that opens a gaping hole [3] in the federal regulatory structure. I cannot support a decision to jettison a cross-border regime that has not proven unreasonable, inflexible, or ineffective in favor of an approach that fails to address the most critical concerns that the Dodd-Frank Act directed the CFTC to address in favor of ''*more workable*'' [4] solutions. As the Final Rule opts to address the conflicts of economic interest between the regulated and those who are advantaged by it [5] by usurping Congressional (and congressionally delegated) authority to rethink section 2(i) of the Commodity Exchange Act (''CEA'' or ''Act'') via prescriptive rules, I must respectfully dissent.

Almost ten years ago to the day, Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act as a legislative response to the 2008 financial crisis. Driven by a series of systemic failures, the crisis laid bare that the essentially unregulated and unmonitored over-the-counter derivatives or ''swaps'' markets were not the bastions of efficiency, stability, and resiliency they were thought to be.[6] Title VII of the Dodd-Frank Act gave the Commission new and broad authority to regulate the swaps market to address and mitigate risks arising from swap activities.[7]

Although much of the over-the-counter derivatives market's contributions to the 2008 financial crisis completed their journey within the continental U.S., the risk originated in foreign jurisdictions.[8] Accordingly, Congress provided in CEA section 2(i) that the provisions of Title VII, as well as any rules or regulations issued by the CFTC, apply to cross-border activities when certain conditions are met.[9]

The D.C. District Court recognized that ''Section 2(i) operates independently, without the need for implementing regulations, and that the CFTC is well within its discretion to proceed by case-by-case adjudications, rather than rulemaking, when applying Section 2(i)'s jurisdictional nexus.'' [10] The D.C. District Court also found that, because the Commission was ''not required to issue *any* rules (let alone binding rules) regarding its intended enforcement policies pursuant to Section 2(i),'' the CFTC's decision to issue the Guidance as a non-binding policy statement benefits market participants.[11] To the extent the CFTC interpreted the meaning of CEA section 2(i) in its 2013 cross-border Guidance, an interpretation carried forward in the Final Rule today (and in its proposal), such interpretation is permissibly drawn linguistically from the statute and, regardless, cannot substantively change the legislative reach of section 2(i) or the Title VII regime.[12] In this regard, the interpretation reinforces the direct meaning of CEA section (2)(i)'s grant of authority—without implementing regulations—to enforce the Title VII rules extraterritorially whenever activities ''have a direct and significant connection with activities in, or effect on, commerce of the United States.'' [13] Putting aside the anti-evasion prong in CEA section 2(i)(2), it remains that CEA section 2(i) applies the swaps provisions of the CEA to certain activities, viewed in the class or aggregate, outside the United States, that meet either of two jurisdictional nexuses: (1) A direct and significant effect on U.S. commerce; or (2) a direct and significant connection with activities in U.S. commerce, and through such connection, present the type of risks to the U.S. financial system and markets that Title VII directed the Commission to address.[14]

The Dodd-Frank Act's derivatives reforms contemplate that an individual entity's systemic riskiness is a product of the interrelations among its various activities and risk-management practices. As a result, the post-crisis reforms target the activity of derivatives trading as a means to reach those entities that conduct the trading.[15] As the Commission has acknowledged, ''Neither the statutory definition of 'swap dealer' nor the Commission's further definition of that term turns solely on risk to the U.S. financial system.'' [16] And to that end, ''[T]he Commission does not believe that the location of counterparty credit risk associated with a dealing swap—which . . . is easily and often frequently moved across the globe—should be determinative of whether a person's dealing activity falls within the scope of the Dodd-Frank Act.'' [17] By adopting an overarching risk-based approach to cross-border regulation today, the Commission jeopardizes the integrity and soundness of the markets it regulates. The Final Rule acknowledges that systemic risk may derive from the activities of entities that do not individually generate the kind of risk that

[1] The Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111–203, 124 Stat. 1376 (2010) (''Dodd-Frank Act'').

[2] *SIFMA* v. *CFTC,* 67 F.Supp.3d 373 (D.D.C. 2014).

[3] *See generally Gonzales* v. *Raich,* 545 U.S. 1 (2005) (relied on by the Commission in the Final Rule at 1.D.2.(i) and in the Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swaps Regulations, 78 FR 45292, 45300 (Jul. 26, 2013) (''Guidance'') to support its interpretation of the Commission's cross-border authority over swap activities that as a class, or in the aggregate, have a direct and significant connection with activities in, or effect on, U.S. commerce—whether or not an individual swap may satisfy the statutory standard.).

[4] *See, e.g.,* Final Rule at II.C.3.

[5] *See Wickard* v. *Filburn,* 317 U.S. 111, 129 (1942).

[6] *See SIFMA,* 67 F.Supp.3d at 385–86 (citing *Inv. Co. Inst.* v. *CFTC,* 891 F.Supp.2d 162, 171, 173 (D.D.C. 2012), *aff'd,* 720 F.3d 370 (D.C. Cir. 2013)).

[7] *See* Guidance, 78 FR at 45299.

[8] *See* Guidance, 78 FR at 45293–45295; *see also SIFMA,* 67 F.Supp.3d at 387–88 (describing the ''several poster children for the 2008 financial crisis'' that demonstrate the impact that overseas over-the-counter derivatives swaps trading can have on a U.S. parent corporation).

[9] 7 U.S.C. 2(i).

[10] *SIFMA,* 67 F.Supp.3d at 423–25, 427; (''Although many provisions in the Dodd-Frank Act explicitly require implementing regulations, Section 2(i) does not.'').

[11] *Id.* at 423 (citation omitted).

[12] *Id.* at 424.

[13] *Id.* at 426.

[14] *See* Proposal at C.1.; Guidance, 78 FR at 45292, 45300; *see also SIFMA,* 67 F.Supp.3d at 424–25, 428 n. 31 (finding that Congress addressed issue of determining which entities and activities are covered by Title VII regulations, ''For Congress already addressed this 'important' issue by defining the scope of the Title VII Rules' extraterritorial applications in the statute itself.'').

[15] *See* Jeremy Kress et al., Regulating Entities and Activities: Complimentary Approaches to Nonbank Systemic Risk, 92 S. Cal. L. Rev. 1455, 1459–60, 1462 (Sept. 2019).

[16] Cross-Border Application of the Registration Thresholds and External Business Conduct Standards Applicable to Swap Dealers and Major Swap Participants, 81 FR 71946, 71952 (Oct. 18, 2016) (''2016 Proposal''); *see also* Further Definition of ''Swap Dealer,'' ''Security-Based Swap Dealer,'' ''Major Swap Participant,'' ''Major Security-Based Swap Participant'' and ''Eligible Contract Participant,'' 77 FR 30596, 30597–98 (May 23, 2012) (''SD Definition Adopting Release'') (explaining how the Dodd-Frank Act definitions of ''swap dealer'' and ''security-based swap dealer'' focus on whether a person engages in particular types of activities involving swaps or security based swaps); *id.* at 30757 (In response to questions as to whether the swap dealer definition should appropriately be activities-based or relate to how an entity is classified, Chairman Gensler clarified that, ''The final rule is consistent with Congressional intent that we take an activities-based approach.'').

[17] 2016 Proposal, 81 FR at 71952.

would subject them to systemic risk-based regulation, but then chooses not to address that very risk. When the CFTC focuses its regulatory oversight only on individually systemically significant entities, it unavoidably leaves risky activities unregulated that due to the interconnectedness of global markets individually, and in the aggregate, can and likely will negatively impact U.S. markets.[18]

Moreover, Congress embedded a risk-based approach, appropriate to the Commission's mandate, within the Dodd-Frank Act's swap dealer definition by instructing the Commission to exempt from designation as a dealer a person that ''engages in a *de minimis* quantity of swap dealing in connection with transactions with or on behalf of its customers'' and providing that an insured depository institution is not to be considered a swap dealer ''to the extent it offers to enter into a swap with a customer in connection with originating a loan with that customer.'' [19] The swap dealer definition further provides that a person may be designated as a dealer for one or more types, classes or categories of swaps or activities without being designated a dealer for other types, classes, or categories of swaps or activities,[20] further indicating that the type and level of risk a particular person's activities present are the guiding factor in determining whether they may be required to register with the Commission as an SD and comply with the requirements of Title VII. The Commission seems to have lost sight of the fact that the activity of swap dealing itself presents the type of risk addressed by Title VII.[21] The Commission's ability to establish a threshold amount of such activity that warrants direct oversight via registration does not diminish this underlying trait, which is not binary, but a measure of the scale of risk. Risk is simply in the DNA of an SD.

As recognized by the Commission, requiring registration and compliance with the requirements of the Dodd-Frank Act reduces risk and enhances operational standards and fair dealing in the swaps markets.[22] To the extent the Dodd-Frank Act was enacted to reduce systemic risk to the financial system, the CFTC's role is to individually utilize its expertise in addressing risk to the financial system created by interconnections in the swaps market as a market conduct regulator through supervisory oversight of SDs and MSPs,[23] and to contribute as a voting member in support of the broader systemic risk oversight carried out by the Financial Stability Oversight Council (''FSOC'').[24]

Since 2013, when the Commission announced its first cross-border approach in flexible guidance as a non-binding policy statement,[25] the Commission has understood that the global scale of the swap markets and domestic scale of regulation poses significant challenges for regulators and market participants.[26] I dissented from the December 2019 proposal for the Final Rule the Commission considers today.[27] Like the Final Rule, the Proposal suggested that we can resolve all complexities in one fell swoop if we alter our lens, abandon our longstanding and literal interpretation of CEA section 2(i), and limit ourselves to the purely *risk-based approach* described therein.

Today's action ignores that, ''It is the essence of regulation that it lays a restraining hand on the self-interest of the regulated and that the advantages from the regulation commonly fall to others.'' [28] The Final Rule is essentially the Proposal with a more clearly articulated intention to rethink the Commission's mandate under the Dodd-Frank Act to seize the status of primary significant risk regulator—a position the Commission was neither delegated to assume nor provided the resources to occupy—so as to limit the application of Title VII. Like the Proposal, the Final Rule acknowledges the likelihood that the chosen course will result in increased risks of the kind Title VII directs us to address flowing into the U.S., or even originating in the U.S. via ANE activities, and then states a belief that the chosen approach is either ''adequate'' [29] or of no moment because our focus on significant participants in the U.S. market should ensure the appropriate persons are subject to Commission oversight via registration, even if, ''to the extent that a registered SD or MSP relies on the exceptions in the Final Rule, and is located in a jurisdiction that does not have comparable swap requirements, the Final Rule could lead to weaker risk management practices for such entities.''.[30] This approach boils down to: ad hoc harmonizing with the Securities and Exchange Commission (''SEC''); de facto delegating to the U.S. prudential regulators; or deferring to a foreign jurisdiction under a banner of comity without ever explaining how the application of the swap dealer *de minimis* registration threshold is unreasonable.

In various statements throughout the preamble, the Commission subtly—and not so subtly—promotes its emergent ''desire to focus its authority on potential significant risks to the U.S. financial system.'' [31] In one glaring instance, the Commission responds to a very clear comment on the weakness of the SRS definition in terms of addressing evasion and avoidance concerns by eviscerating Congress's very carefully crafted SD definition, stating, ''[w]ithout this risk-based approach [SRS], the SD de minimis threshold, which is a strictly activity-based test (*i.e.,* a test based on the aggregate gross notional amount of dealing activity), becomes the de facto risk test of when an entity would be subject to the Commission's swap requirements as an SD.'' [32] In the past several years, I have noted the Commission's eagerness to bypass clear Congressional intent in order to address longstanding concerns with Dodd-Frank Act implementation.[33] Indeed, the Commission has at times made a concerted effort to avoid targeted amendments in favor of sweeping changes to the regulation of swap dealers without regard for the long term consequences of its fickle interpretation of the law and analysis of risk.[34] I have grave concerns that the Final Rule's motive in commandeering the role of systemic risk regulator is to provide certainty to entities that they will have sufficient paths in the future to avoid registration with the Commission, and thus fly under the radar of the FSOC and the entire Title VII regime. As the DC District Court noted, the Commission cannot second-guess Congress' decision that Title VII apply extraterritorially.[35] In layering its new approach over the CEA section 2(i) analysis, the Commission does just that.

My dissent to the Proposal expounded at length on concerns with the Commission's ''new approach,'' which seeks to improve upon and clarify the Guidance while reallocating responsibilities in a manner that

[18] *See* Guidance, 78 FR at 45300 (consistent with relevant case law and the purpose of Title VII to protect the U.S. financial system from the build-up of systemic risks, under CEA section 2(i), the Commission must assess the connection of swap activities, viewed as a class or in the aggregate, to activities in commerce of the United States to determine whether application of the CEA swaps provisions is warranted).

[19] *See* CEA section 1a(49)(C) through (D), 7 U.S.C. 1a(49)(C) through (D).

[20] *See* CEA section 1a(49)(B), 7 U.S.C. 1a(49)(B).

[21] *See* Final Rule at II.D.3.(iv) (identifying the SD *de minimis* threshold as ''a strictly activity-based test (*i.e.,* a test based on the aggregate gross notional amount of dealing activity).

[22] *See* SD Definition Adopting Release, 77 FR at 30599.

[23] *See* Press Release Number 8033–19, CFTC, CFTC Orders Six Financial Institutions to Pay Total of More Than $6 Million for Reporting Failures (Oct. 1, 2019), *https://www.cftc.gov/PressRoom/PressReleases/8033-19* (''The Commission's swap-dealer risk management rules are designed to monitor and regulate the systemic risk endemic to the swaps marke.t''); *see also,* Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies, 84 FR 71740, 71744 (Dec. 30, 2019) (explaining that the activities-based approach to identifying, assessing, and addressing potential risks and threats to U.S. financial stability reflects two priorities, one of which is ''allowing relevant financial regulatory agencies, which generally possess greater information and expertise with respect to company, product, and market risks, to address potential risks, rather than subjecting companies to new regulatory authorities.'').

[24] Among other things, the FSOC is authorized to ''issue recommendations to the primary financial regulatory agencies to apply new or heightened standards and safeguards.'' Dodd-Frank Act section 120, 124 Stat. at 1408–1410.

[25] *See* Guidance, 78 FR at 45292.

[26] *See* Hannah L. Buxbaum, *Transnational Legal Ordering and Regulatory Conflict: Lessons from the Regulation of Cross Border Derivatives,* 1 U.C. Irvine J. Int'l Transnat'l & Comp. L. 91, 92 (2016).

[27] *See* Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants, 85 FR 952, 1008 (proposed Jan. 8, 2020) (the ''Proposal'').

[28] *Wickard* v. *Filburn,* 317 U.S. 111.

[29] *See, e.g.,* Final Rule at II.D.3.(iii)–(iv).

[30] Final Rule at X.C.11.(iv).

[31] *See* Final Rule at V.C.

[32] *See* Final Rule at II.D.3.(iv).

[33] *See, e.g.,* De Minimis Exception to the Swap Dealer Definition—Swaps Entered into by Insured Depository Institutions in Connection With Loans to Customers, 84 FR 12450, 12468–12471 (Apr. 1, 2019).

[34] *See, e.g., id.;* Segregation of Assets Held as Collateral in Uncleared Swap Transactions, 84 FR 12894, 12906 (Apr. 3, 2019); De Minimis Exception to the Swap Dealer Definition, 83 FR 27444 (proposed June 12, 2018).

[35] *SIFMA,* 67 F.Supp.3d at 432.

is ill-conceived given that we are just 10 years past one crisis, and currently navigating a global pandemic. Accordingly, I will not reiterate my earlier points, but incorporate by reference my prior dissent,[36] which is still on point save for a comment I made on the ''unlimited U.S. responsibility prong'' to the U.S. person definition, which has been addressed, and I thank staff for addressing my concern.[37] I will, however, take the opportunity here to focus on how the Commission's approach to the cross-border application of the SD registration threshold in the Final Rule amounts to a re-write of the Dodd-Frank Act, as exemplified by the ''significant risk subsidiary'' or ''SRS'' definition.

The Commission Does Not Have a Blank Check

By codifying a purely and defined risk-based approach to its extraterritorial jurisdiction, exempting from the CFTC's regulatory oversight all entities but those which individually pose systemic risk to the U.S. financial system, the CFTC abdicates its Congressionally-mandated responsibility under CEA section 2(i) to regulate activities outside of the United States that meet one of the aforementioned jurisdictional nexuses.[38] The Final Rule today defies Congress' clear intent in enacting CEA section 2(i), improperly elevates comity over adhesion to the CFTC's mandate, and increases the riskiness of global swap markets.

Congress demonstrated its ability to discern between purely systemic risk-based and activities-based regulation when it designated authority to the CFTC. It directed the Commission to develop a metric to analyze which entities pose enough risk to require SD registration, creating an exception to the registration requirement for entities engaged in only a *de minimis* quantity of swap dealing.[39] It is telling that the CEA does not, under section 2(i), direct the CFTC to develop a similar threshold measurement to evaluate whether foreign entities singularly pose systemic risk to U.S. commerce. The lack of a comparable exception in CEA section 2(i) indicates that Congress intended to do exactly what the plain language of CEA section 2(i) suggests—require that the CFTC oversee *activities* outside of the U.S. that pose risk to U.S. commerce (not individual persons or entities). [40] Furthermore, nothing in the swap dealer definition or CEA section 2(i) expresses that we should defer to prudential regulators, whether U.S. or foreign; prudentially-regulated entities may be required to register as swap dealers with the CFTC.[41] If the Congress believed that prudential regulation could sufficiently mitigate risk to the U.S. financial system, it would have chosen to delegate this function to the U.S. prudential regulators. Congress instead chose to enact a registration requirement in Title VII of the Dodd-Frank Act. Ultimately, the introduction of the concept of an ''SRS'' and accompanying exemptions for: (1) Entities with parents that have less than $50 billion in consolidated assets, and for entities that are already (2) prudentially regulated or (3) subject to comparable foreign regulation, is impermissible under CEA section 2(i).

Whether or not we agree with Congress, the CFTC is not free to rewrite the statute and enact rules that contravene our mandate. Agencies may not act like they have a ''blank check'' to proffer legislative rules outside of their delegated authority; [42] regulators have to take directives from their governing statute and not second-guess Congress.[43] Thus, the CFTC is not free to disregard its mandate in the pursuit of other objectives—such as comity, deference, adequacy, workability, or an inexplicable desire to act solely like a prudential regulator—no matter how laudable some of those objectives might be.[44] The Commission today dodges the responsibility with which it was entrusted in the wake of a crisis, impermissibly rewriting the Dodd-Frank Act to pass the buck to prudential regulators and our international counterparts.

The CFTC's implementation of the Final Rule's purely risk-based approach to regulating global swaps is neither allowable under Title VII, nor is it wise. Our current Chairman, in fulfilling his role as the CFTC's representative on the FSOC, when supporting guidance signifying that the FSOC would adopt an activities-based approach to determining risks to financial stability, stated that an entity-based approach, ''inevitably leads to a 'whack-a-mole' scenario in which risky activities are transferred out of highly-regulated entities and into less-regulated ones.'' [45] Given the conglomeration of exceptions built into the Final Rule's definitions of ''guarantee,'' and ''SRS,'' and its determination regarding ''ANE Transactions,'' it is hard to see how this transfer of risk to less-regulated entities—which still pose risk in the aggregate to U.S. markets—will not come to pass, inevitably leaving gaps in the CFTC's ability to oversee the activities it regulates.

With respect to our cooperation with foreign counterparts, I firmly believe that the CFTC should work diligently to coordinate oversight and elevate principles of international comity as we develop our cross-border approach—but not when doing so requires us to abdicate our mandate. To that end, I generally support the Final Rule's application of substituted compliance even if I do not fully agree with entity categorizations via the definitions. I also generally support the CFTC's deference to foreign regulators when it makes sound comparability determinations. To the extent the Final Rule grants somewhat indeterminate discretion to the CFTC to depart from an objective evaluation in making such determinations, as noted by several commenters,[46] I will remain vigilant when participating in such Commission action and be mindful of potential for slippage.

I remain concerned that the Final Rule, like the Proposal, makes vague references to ''comity'' to justify our resistance to regulating overseas activities that pose risk to U.S. markets. I agree that making substituted compliance available to foreign entities or subsidiaries, via sound comparability determinations, is appropriately deferential to principles of international comity. Nevertheless, we should only use comity to justify rulemaking when there is ambiguity in the governing statute,[47] or when our requirements unreasonably interfere with those of our international counterparts [48]—neither of which is overtly true regarding our statutory obligation under CEA sections 4s(a) and (c) [49] to register SDs and MSPs based on

[36] *See* 85 FR at 1009–1013.

[37] *Id.* at 1011.

[38] *See* 7 U.S.C. 2(i).

[39] *See* CEA section 1a(49)(D); 7 U.S.C. 1a(49)(D).

[40] *Silvers* v. *Sony Pictures Entm't, Inc.,* 402 F.3d 881, 885 (9th Cir. 2005) (''The doctrine of expressio unius est exclusio alterius 'as applied to statutory interpretation creates a presumption that when a statute designates certain persons, things, or manners of operation, all omissions should be understood as exclusions.''' (quoting *Boudette* v. *Barnette,* 923 F.2d 754, 756–57 (9th Cir. 1991)).

[41] *See also* CEA section 4s(c), 7 U.S.C. 4s(c) (requiring any person that is required to register as a swap dealer or major swap participant to register with the Commission, ''regardless of whether the person also is a depository institution or is registered with the Securities and Exchange Commission.'').

[42] Neomi Rao, Address at the Brookings Institution: What's next for Trump's regulatory agenda: A conversation with OIRA Administrator Neomi Rao (Jan. 26, 2018), Transcript at 10 (''. . .agencies should not act as though they have a blank check from Congress to make law.''), *https://www.brookings.edu/wp-content/uploads/2018/01/es_20180126_oira_transcript.pdf.*

[43] *See SIFMA,* 67 F.Supp.3d at 432 (finding that the CFTC ''could not have second-guessed Congress decision'' that Title VII rules apply extraterritorially).

[44] *BP W. Coast Prods., LLC* v. *FERC,* 374 F.3d 1263 (DC Cir. 2004) (Congressional mandates to agencies to carry out ''specific statutory directives define[ing] the relevant functions of [the agency] in a particular area.'' Such a mandate does not create for the agency ''a roving commission'' to achieve those or ''any other laudable goal.'' (quoting *Michigan* v. *EPA,* 268 F.3d 1075, 1084 (DC Cir. 2001)); *see also Farmers Union Cent. Exch., Inc.* v. *FERC,* 734 F.2d 1486, 1500 (DCC. 1984) (''Agency decisionmaking, of course, must be more than 'reasoned' in light of the record. It must also be true to the Congressional mandate from which it derives authority.'').

[45] Heath P. Tarbert, Chairman, CFTC, Statement on the New Activities-Based Approach to Systemic Risk (Dec. 19, 2019), *https://www.cftc.gov/PressRoom/SpeechesTestimony/tarbertstatement120619.*

[46] *See* Proposal at VI.D.1.(ii.).

[47] Michael Greenberger, *Too Big to Fail—U.S. Banks' Regulatory Alchemy: Converting an Obscure Agency Footnote into an ''At Will'' Nullification of Dodd-Frank's Regulation of the Multi-Trillion Dollar Financial Swaps Market,* 14 J. Bus. & Tech. L. 197, 367 (2019) (''There is no legal precedent extant that defines 'international comity' as giving authority to a U.S. administrative agency to weaken unilaterally the otherwise clear Congressional statutory language or intent that the statute must be applied extraterritorially.'')

[48] *See* Proposal, 85 FR at 957; Final Rule at II.D.3.(iv); Aaron D. Simowitz, *The Extraterritoriality Formalisms,* 51 Conn. L. Rev. 375, 405–6 and n. 205 (2019) (describing the principle of ''prescriptive comity'' in the Restatement (Fourth) of Foreign Relations Law and recognizing that ''Interference with the sovereign authority of foreign states may be reasonable if such application would serve the legitimate interests of the United States.'' (citing Restatement (Fourth) of Foreign Relations Law § 405 cmt. (Am. Law. Inst. 2018)).

[49] CEA section 4s(a), (c), 7 U.S.C. 4s(a), (c).

their swap activities. Registration is a critical first step in determining whether a non-U.S. entity is engaged in activities covered under 2(i), and must not be disregarded for the sake of comity.

It is also pertinent to note here that by prioritizing comity and refusing to appropriately retain jurisdiction, at least to some degree, over transactions that are arranged, negotiated, or executed in the United States by non-U.S. SDs with non-U.S. counterparties (''ANE Transactions''), the Commission's abdication of Congressionally-mandated responsibility extends beyond CEA section 2(i). There is no need to even address whether these transactions have a ''direct and substantial'' impact on U.S. commerce, because they occur *in* the United States and accordingly fall squarely within the regulatory purview of the CFTC.[50] Ignoring all ANE Transactions invites entities to evade U.S. law, even as they avail themselves of the benefits of U.S. markets by residing in the U.S. and using U.S. personnel, as they can administratively treat transactions as booked in a foreign subsidiary based on the conclusion that any relevant risk has been shipped off. I am concerned that the CFTC is improperly fixating on comity at the expense of not only its mandate, but also at the expense of developing sound regulation that increases transparency, competition, and market integrity. The Final Rule brushes past concerns raised by a market participant that exempting ANE transactions from reporting requirements gives non-U.S. entities an advantage over U.S. SDs and jeopardizes the intended benefits of the CFTC's public reporting regime.[51] I am concerned by the Commission's response to the comment,[52] and I struggle to understand why any U.S. regulator would implement a rule that defies its statutory mandate, subjects U.S. entities to a competitive disadvantage relative to its foreign counterparts, and reduces U.S. investors' transparency into the markets.

SRS: This Is the Way

In my dissent to the Proposal, I identified SRS as the most elaborate departure from both the Commission's interpretation of CEA section 2(i) and from our mandate under the Dodd-Frank Act, in its elimination of a large cross-section of non-U.S. subsidiaries of U.S. parent entities from having to count their swap dealing activities toward the relevant SD or MSP registration threshold calculations.[53] The SRS replaces the conduit affiliate concept from the Guidance, which, although broader, served to (1) appropriately define the universe of entities whose risks related to swap activities may accrue and have a direct and significant connection with activities in, or effect on, U.S. commerce, and (2) harmonize with the SEC's cross-border application of the *de minimis* threshold relevant to security-based swap dealing activity.[54]

Despite a clear split among Commissioners and commenters, the Commission has determined to move forward with the SRS, which creates broad exceptions that could exclude large amounts of the swap dealing activities by foreign subsidiaries of U.S. entities from counting towards the SD and MSP registration threshold calculations and therefore, ultimately exclude them from the Commission's oversight and application of the swap dealer regulations. In support of its determination, the Commission rehashes and repeats the argument that SRS ''embodies'' the Commission's purely risk-based approach.[55] If ''this is the way,''[56] then I am afraid our new approach may not account—perhaps at all—for the risk that Congress and the Dodd-Frank Act directed the Commission to oversee. If Congress had wanted the Commission to focus its cross-border authority solely on systemically significant non-bank entities, it would have been explicit, and refrained from using language in CEA section 2(i) that was so embedded in common law.[57]

In excluding subsidiaries of bank holding companies and intermediate holding companies from the SRS definition, the Commission defers to the ''role of prudential regulation in the consolidated oversight of prudential risk,'' again relying on ''the risk-based approach to determining which foreign subsidiaries present a significant risk to their ultimate U.S. parent and thus to the financial system.''[58] In presuming that prudential oversight provides ''sufficient'' comparable oversight to that prescribed by Title VII, the Commission entirely ignores that history weighs against such a presumption[59] and Congress acted accordingly.[60] Under the Dodd-Frank Act, the CFTC is the ''primary financial regulatory agency'' for swap dealers.[61] CEA section 4s(c)[62] provides that any person that is required to be registered as an SD or MSP shall register with the CFTC regardless of whether the person also is a depository institution (*i.e.,* any bank or savings association) or is registered with the SEC as a security-based swap dealer. Moreover, to the extent SDs or MSPs have a prudential regulator, Title VII recognizes that such SDs/MSPs are to comply with capital and margin requirements established by their respective prudential regulators.[63] However, it explicitly does not recognize prudential regulation as a substitute for SD/MSP regulatory oversight by the Commission.[64]

Again, I believe that our cross-border approach must absolutely align with principles of international comity and that our rules and supervisory approach should harmonize and work in tandem with prudential regulation. However, I do not believe that the SRS definition is reasonable or consistent with the SD definition or CEA section 2(i), due to its deference to the role of prudential regulation in the consolidated oversight of prudential risk to carve out consideration of swap dealing activities of non-U.S. entities (that are not guaranteed by a U.S. person) for purposes of SD registration and Commission oversight.

The Final Rule would suggest that our consideration of the activities of non-U.S. subsidiaries of U.S. entities is an ''expansion'' of the Commission's oversight.[65] I disagree. The post-2010 crisis reforms require intensive oversight of entities engaged in swaps activities throughout the world. The Commission must retain in full

[50] *See SIFMA,* 67 F. Supp. 3d at 426 (''Section 2(i)'s ''technical language initially lays down a general rule placing all [swap] activity'' occurring outside of the United States beyond Title VII's reach. But it then expressly brings such swap activities ''back within'' Title VII's purview). ANE Transactions should not be a part of the initial exemption step required by section 2(i), because they do not occur outside of the United States.

[51] *See* Proposal at V. B.-C.; Citadel, Comment Letter on Proposed Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants (Mar. 9, 2020), *https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=62376.*

[52] *See SIFMA,* 67 F. Supp. 3d at 429 (An agency '''need not address every comment, but it must respond in a reasoned manner to those that raise significant problems.' ''(citing *Covad Commc'ns Co.* v. *FCC,* 450 F.3d 528, 550 (D.C. Cir. 2006) (quoting *Reytblatt* v. *Nuclear Regulatory Comm'n,* 105 F.3d 715, 722 (D.C. Cir. 1997))).

[53] 85 FR at 1012; *see also* Dissenting Statement of Commissioner Dan M. Berkovitz, 85 FR at 1015 (describing the SRS construct as ''an empty set.'').

[54] *See* 17 CFR 240.3a71–3(a)(1).

[55] See Final Rule at II.C. 3.(iii) (in declining to incorporate risk transfer and risk acceptance test into the ''significant subsidiary'' definition, the Commission finds that such activity-based tests are inconsistent with the Commission's determination to apply swap requirements to foreign entities using a risk-based test to isolate entities that the Commission considers to pose a significant risk to the financial system based solely on their significance in terms of their balance sheet size relative to the parent entity).

[56] ''This is the way'' is identified as a Mandalorian mantra and cultural meme associated with keeping members of the group on the same wavelength without any question at all. *See* Evan Romano, *What 'This Is the Way' Explains About the Mandalorians in The Mandalorian,* Men'sHealth (Nov. 22, 2019).

[57] *See, e.g.* Proposal at I.C.1.; Guidance 81 FR at 45298–45300; *see SIFMA,* 67 F.Supp.3d at 427 (''Congress modeled Section 2(i) on other statutes with extraterritorial reach that operate without implementing regulations.'' (citations omitted)); *see* Larry M. Eig, Cong. Research Serv., 97–589, Statutory Interpretation: General Principles and Recent Trends 20 (2014) (Congress is presumed to legislate with knowledge of existing common law.'').

[58] Notably, the Commission determined to use the $50 billion threshold for the ultimate parent entity of an SRS because the FSOC initially used a $50 billion total consolidated assets quantitative test as one threshold to apply to nonbank financial entities for purposes of designated nonbank financial companies as ''systemically important financial institutions'' (''SIFIs''). *See* Proposal, 85 FR at 965 n.134. The FSOC recently voted to remove the $50 billion threshold because, among other things, it was ''not compatible with the prioritization of an activities-based approach'' to addressing risks to financial stability. *Id.;* see also FSOC Interpretive Guidance, 84 FR at 71742.

[59] *See, e.g.,* Guidance, 78 FR at 45294; Proposal, 85 FR at 1013–1015.

[60] *Id.*

[61] Dodd-Frank Act, Public Law 111–203 section 2(12)(C)(viii), 124 Stat. 1389.

[62] CEA section 4s(c), 7 U.S.C. 4s(c).

[63] CEA section 4s(e)(2)(A), 7 U.S.C. 4s(e)(2)(A)

[64] *See* Eig, *supra* note 57 at 16–17 (''where Congress includes particular language in one section of a statute but omits it in another . . . , it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.'' (quoting *Atlantic Cleaners & Dyers, Inc.* v. *United States,* 286 U.S. 427, 433 (1933))).

[65] Final Rule at II. D. 3. (iv).

its oversight and regulatory responsibilities over entities whose activities have a direct and significant connection with activities in, or effect on, U.S. commerce. To do that effectively, we must be able to apply the SD definition and *de minimis* threshold to the web of interconnections through which risk travels, not simply rely on bright line balance sheet box checking to wholesale elimination of non-U.S. subsidiaries from our scope of consideration. As I stated in my prior dissent, without a more concrete understanding as to whether SRS is truly superior to the conduit affiliate [66] concept currently outlined in the Guidance and presumably similar to the SEC's own approach, it is difficult to get behind a policy that would bring risk into the U.S. of the very type CEA Section 2(i) seeks to address.

Complexity and Burden Should Not Direct the Outcomes

I continue to have reservations regarding the Commission's determination to discard the Guidance and the use of agency guidance and non-binding policy statements in favor of prescriptive rules.[67] As I noted with regard to the Proposal, while the Guidance is complex, it is no more complex than this Final Rule. Complexity is the hallmark of the regulation of cross-border derivatives, and ''merely reflects the complexity of swaps markets, swaps transactions, and the corporate structures of the market participants that the CFTC regulates.'' [68] I am especially concerned that the Commission is acting in haste to nail down hard and fast rules while many pieces in the global regulatory puzzle are still in flux.

Commenters refrained from weighing in on the virtues of retaining the Guidance—or agency guidance generally. The Proposal garnered just 18 relevant comment letters.[69] It is difficult to determine why, but perhaps market participants have followed the Guidance and utilized their expertise in reviewing the overall statutory scheme and the straightforward language of CEA section 2(i) to come into compliance with Title VII either directly or via substituted compliance and have not found it prohibitive to do so.[70]

[66] *See, e.g.,* 85 FR at 1012 (noting the Proposal's lack of explaining whether and how the conduit affiliate concept failed to achieve its purpose, is no longer relevant, resulted in loss of liquidity or market fragmentation, proved unworkable, etc.).

[67] *Id.* at 1010.

[68] *SIFMA,* 67 F.Supp.3d at 419–20 (''Indeed, the complexity of a regulatory issue is one reason an agency might choose to issue a non-binding policy statement rather than a rigid 'hard and fast rule.' '' (citing *SEC* v. *Chenery Corp.,* 332 U.S. 194, 202–203 (1947))).

[69] Comments to the Proposal are available at *https://comments.cftc.gov/PublicComments/CommentList.aspx?id=3067.* Of note, the proposal to the Guidance received approximately 290 comment letters. Guidance, 78 FR at 45295. The 2016 Proposal received approximately 29 substantive comment letters, available at *https://comments.cftc.gov/PublicComments/CommentList.aspx?id=1752.*

[70] Indeed, the DC District Court concluded that the CFTC need not address every facet of the overall regulatory scheme and can rely on regulated market participants to reference other controlling statutes and regulations to address issues left unresolved by a given Title VII rule. *See SIFMA,* 67 F. Supp. 3d at 428 n.31.

Like the Proposal, the Final Rule prides its alteration of various definitions such as ''U.S. person'' and ''guarantee,'' the substitution of SRS for conduit affiliates, and the abandonment of ANE Transactions, as burden and/or cost reducing (or, ''more workable''). Unfortunately, I believe the Commission in some instances has not fully evaluated the true weight of the burdens, and in other instances, not fully measured those burdens against the goals of Title VII and the benefits of the overall intent of CEA section 2(i).

A straightforward example is the Commission's determination to increase the proposed five-year time limits for reliance on representations regarding U.S. person and guarantee status to seven years to appease commenters who asked for perpetual reliance on previously obtained representations.[71] There is no indication that the Commission considered anything but providing market participants more time, in spite of recognizing that best practice would be to obtain updated representations as soon as practicable.

A more concerning example is the Commission's decision to move forward with a narrower definition of ''guarantee'' than that outlined in the Guidance, despite recognizing that it could lead to entities counting fewer swaps towards their *de minimis* registration threshold or ''qualify additional counterparties for exceptions to certain regulatory requirements as compared to the definition in the Guidance.'' [72] The Commission did not address the commenter who also pointed out that the narrower definition would allow significant risk to be transferred back to the U.S. financial system over time noting that, ''economic implications are just as important as legal considerations, as confirmed and intended by CEA section 2(i)(1).[73] Instead, the Final Rule offers the possibility that the SRS definition would capture some non-U.S. persons, returning to the mantra that in this way we focus on those entities that represent ''material risk to the U.S. financial system,'' through something ''workable.'' [74]

Conclusion

Before I conclude, I would like to take a moment to thank staff from the Division of Swap Dealer and Intermediary Oversight for their presentations, tireless work on this rulemaking, and frequent engagement with my office over the last few weeks leading up to today's open meeting. Like all of the CFTC's work, today's discussion would not have been possible without the expertise and commitment of our dedicated staff.

As the Commission wraps up its scheduled work, before a brief summer respite, particularly on this 10th anniversary week of the Dodd-Frank Act, our work yesterday and today, although some may like to think it, is *not* the culmination of years of work towards implementing the Dodd-Frank Act. In fact, the Commission acted promptly in issuing the cross-border 2013 Guidance, only a few

[71] *See* Final Rule at II.B.5. and C.3.

[72] *See* Final Rule at II.C.2. and 3.

[73] *Id.*

[74] *See* Final Rule at II.C.3.

years after bill passage and in the throes of dozens of other equally important Title VII rulemakings.

This week's exercise is a retrenchment of sound derivatives policy that provided the CFTC the tools necessary to monitor swap markets and protect the U.S. financial system and American taxpayers, and most importantly was steadfast to clearly articulated Congressional intent. There is always room for improvement, tweaking, and evolving—I have said as much, many times since becoming a Commissioner.

But, unfortunately, during this week that we should be lifting up the merits of financial reform, especially given the role post-crisis reforms played in absorbing massive shocks during the worst of the Covid–19 pandemic just a few months ago, we are turning back the clock to a previous era that proved to be inadequate to meeting our core responsibilities.

Appendix 5—Statement of Commissioner Dawn D. Stump

Overview

When we met together in person late last year to consider proposing cross-border rules with respect to registration thresholds and regulatory requirements applicable to swap dealers and major swap participants (the ''Proposal''),[1] I stressed that because we were proposing to replace the Commission's 2013 cross-border guidance (the ''Guidance'') [2] with binding and enforceable rules, those rules must be clear, sensible, and workable.[3] In supporting the Proposal at the time, I concluded that the proposed rules met those standards. And I have not seen anything in the many thoughtful comment letters we received that causes me to doubt that conclusion.

The final rules that are before us today, as we meet remotely several months later, are largely the same as those we proposed. But based on public input: (1) In several places, we are providing clarifications requested by market participants; [4] (2) in a few places where the proposal deviated from the Guidance, we have been persuaded that the Guidance got it right, and thus are returning to the Guidance approach; [5] and (3) in still

[1] There are no registered major swap participants at this time. Accordingly, for convenience, this Statement generally will refer only to swap dealers, and not to major swap participants.

[2] Interpretive Guidance and Policy Statement Regarding Compliance With Certain Swap Regulations, 78 FR 45292 (July 26, 2013).

[3] Statement of Commissioner Dawn D. Stump Regarding Proposed Rule: Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants (December 18, 2019), available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/stumpstatement121819.*

[4] *E.g.,* clarification that in addition to entities that are subject to capital regulation by the CFTC, Securities and Exchange Commission (''SEC''), or U.S. prudential regulators, the attribution requirement in connection with the major swap participant registration threshold also excludes entities subject to Basel-compliant capital standards and oversight by a G–20 prudential supervisor.

[5] *E.g.,* addition of a provision that was in the Guidance, but not in the Proposal, whereby a non-

Continued

other places, we are incorporating suggestions made by commenters.[6] As a result, the final rules build and improve upon the foundation laid by the Proposal. They, too, are clear, sensible, and workable, and I am pleased to support them.

I do not plan to summarize here the changes to the Proposal that are encompassed within the final rules. To those not steeped in the minutiae of *de minimis* swap dealer registration calculations and entity- and transaction-level requirements under the Guidance,[7] such a summary can become somewhat mind-numbing. Instead, I would like to place today's cross-border rulemaking in context, and explain my support from a broader perspective.

Section 2(i) and Codifying the Guidance

We begin, as we must, with the terms of the statute—Section 2(i) of the Commodity Exchange Act (''CEA''), which was added by the Dodd-Frank Act.[8] Given the importance of this topic, please indulge my reiterating a few points that I made about the Proposal.

Section 2(i) limits the international reach of CFTC swap regulations by affirmatively stating that they ''shall not apply to activities outside the United States unless those activities . . . have a direct and significant connection with activities in, or effect on, commerce of the United States.'' [9] A common-sense reading of this section is that there is a limited extraterritorial reach to the Dodd-Frank swap requirements, and to stretch them beyond the stated statutory criteria impermissibly infringes upon the rule sets of other nations.

That is, the plainly stated congressional intent is to start with US law not applying beyond our borders, and then continue to the limited conditions where extraterritoriality would be deemed appropriate. The law does not say that CFTC rules govern derivatives market activities around the world if there is *any* linkage or tie to the United States and should not be interpreted and abused as such.

In adopting rules setting out how we will apply Section 2(i) to the registration thresholds and regulatory requirements relevant to the cross-border activities of swap dealers, we are not writing on a blank canvas. The Guidance has been in place for seven years now, and although it is non-binding,[10] market participants (both those that have registered and those that have had to determine whether they are required to register) have devoted a tremendous amount of human and financial resources to conform to its complicated contours.

Faced with that reality, although I was not a fan of the Guidance when it was issued,[11] I agree that it is appropriate to codify its basic elements into our rule set rather than start from scratch. And that is what the final rules before us today will do. The final rules codify many elements of the Guidance, while updating a few provisions to reflect current realities and incorporating some improvements based on our experience during the intervening years.[12]

Much has been made of statements in the Proposal, which are carried over into today's release, that the focus of the Commission's analysis under Section 2(i) is on risk to the U.S. financial system. But this, too, is essentially a codification of the approach taken in the Guidance. While I do not often quote then-Chairman Gary Gensler, I note that in his Statement supporting the adoption of the Guidance, he said:

There's no question to me, at least, that the words of Dodd-Frank addressed this (*i.e.,* risk importation) when they said that a direct and significant connection with activities and/or effect on commerce in the United States covers these risks that may come back to us.

I want to publicly thank Chairman Barney Frank along with Spencer Bachus, Frank Lucas, and Collin Peterson, and their staffs for reaching out to the CFTC and the public to ask how to best address offshore risks that could wash back to our economy in Dodd-Frank.[13]

Implementing our statutory cross-border mandate through a risk-based analysis that focuses on the pertinent issue of risk to the US financial system is a sensible approach, which I endorse.

For those who maintain that the final rules take too narrow a view of the Commission's extraterritorial reach with respect to swap dealers, I note the truly remarkable fact that today, with the Guidance in effect, approximately half of the over 100 swap dealers currently registered with the CFTC are located outside the United States.[14] This percentage has stayed relatively constant since the CFTC's swap dealer registration regime ''went live'' at the end of 2012. Registered non-US swap dealers are located across the globe—in North and South America, Europe, Asia, and Australia.

In other words, although it is non-binding, the Commission's Guidance appears to have brought a substantial portion of global swap dealing activity into the Commission's swap dealer regulatory regime. And the record before us is devoid of evidence suggesting that the number of registered non-US swap dealers is seriously over- or under-inclusive. Given the extent to which the final rules codify the Guidance, a significant change in that number is unlikely.

Because the final rules essentially codify the Guidance, and because I support the final rules for the reasons explained herein, I accept the interpretation of CEA Section 2(i) stated in the Guidance and the final rules in the limited context of registration thresholds and regulatory requirements applicable to swap dealers. To codify the Guidance while revising the foundation on which it was based would only generate confusion—as opposed to the clarity that I hope this rulemaking will bring to one aspect of our cross-border work.

But the analysis of, in Mr. Gensler's words, ''offshore risks that could wash back to our economy'' may well differ in the context of other Dodd-Frank requirements. As we proceed with other aspects of our cross-border work—in areas such as clearing, trade execution, and reporting—rigorous analysis of the Section 2(i) test for each rule we adopt is necessary to ensure that the law is followed both to the letter and in spirit.

Clear, Sensible, and Workable Rules

Transitioning from the interpretation of Section 2(i) to the rules before us, some have questioned why we are adopting rules in the first place. While it is true that Section 2(i), unlike other provisions in Dodd-Frank, does not require the Commission to adopt implementing rules, I believe it is good government to do so. Guidance has its place, of course. Given the nascent state of post-Pittsburgh derivatives reforms in 2013, reliance on guidance made sense at the time. But I have spoken before of the benefits of codifying interpretations issued by our staff where appropriate,[15] and those benefits accrue in equal measure to the codification

U.S. person does not have to count in its *de minimis* swap dealer registration calculation swaps entered into with an entity whose swap obligations are guaranteed by a U.S. person if the guaranteed entity is itself below the *de minimis* threshold and is affiliated with a registered swap dealer.

[6] *E.g.:* (1) While the Proposal removed the prong of the ''U.S. person'' definition in the Guidance that included a legal entity that is majority-owned by one or more U.S. person(s) in which such person(s) ''bears unlimited responsibility for the obligations and liabilities'' of the legal entity, the final rules add such a circumstance to the definition of a ''guarantee;'' and (2) while the Proposal excepted certain subsidiaries of bank holding companies from the definition of a ''significant risk subsidiary,'' the final rules also except certain subsidiaries of intermediate holding companies in the same circumstances.

[7] The final rules replace the Guidance's classification of requirements imposed on registered swap dealers under the Commission's rules as entity- and transaction-level requirements with a similar (but not identical) classification into group A, group B, and group C requirements (discussed further below).

[8] Public Law 111–203, 124 Stat. 1376 (2010) (''Dodd-Frank'').

[9] CEA Section 2(i), 7 U.S.C. 2(i).

[10] *SIFMA* v. *CFTC,* 67 F. Supp.3d 373 (D.D.C. 2014).

[11] When the CFTC was considering the Guidance, I shared the view vividly articulated by then-Commissioner Jill Sommers that the Guidance, as it had been proposed, reflected ''what could only be called the 'Intergalactic Commerce Clause' of the United States Constitution . . .'' *See* Cross-Border Application of Certain Swaps Provisions of the Commodity Exchange Act, 77 FR 41214, 41239 (proposed July 12, 2012) (Statement of Commissioner Sommers).

[12] Several commenters asked the Commission to take the opportunity of this rulemaking to significantly alter the Guidance approach to the cross-border activities of swap dealers in various respects. As noted, we have determined to codify, rather than reconstruct, most of the decisions that underlie the Guidance (although we have made some adjustments as discussed herein). While maintaining the *status quo* under the Guidance may deny affected market participants results they wish for, it does not require them to give up what they have had for the past seven years.

[13] Guidance, 78 FR at 45371 (Statement of Chairman Gary Gensler).

[14] *See* National Futures Association Membership and Directories (data as of July 22, 2020), available at *https://www.nfa.futures.org/registration-membership/membership-and-directories.html#SDRegistry.*

[15] *See* Statement of Commissioner Dawn D. Stump Regarding Amending Rule 3.10(c)(3)—Exemption from Registration for Foreign Persons Acting as Commodity Pool Operators on Behalf of Offshore Commodity Pools (May 28, 2020) (''Commissioner Stump Part 3 Statement''), available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/stumpstatement052820.*

of Commission guidance. Replacing the prior Guidance with rules that reflect current realities and are based on experience developed during the past seven years provides certainty to the marketplace and a shared understanding of the ''rules of the road.''

Some may argue that in those few places where the rules of the road that we are adopting today depart from the Guidance, the Commission has retreated with respect to the extraterritorial application of its swap regulatory regime. As I shall discuss, however, such criticisms fail to take account of other, equally important, considerations relevant to the exercise of our rulemaking authority: (1) The aforementioned need for clear, sensible, and workable rules; and (2) appropriate deference to comparable regimes of our international regulatory colleagues.

Definition of a ''Guarantee''

For example, the release accompanying the final rules acknowledges that the definition of a ''guarantee'' that we are adopting today is narrower than that in the Guidance. The final rules define a ''guarantee'' as an arrangement in which one party to a swap has rights of recourse against a guarantor with respect to its counterparty's obligations under the swap, with ''rights of recourse'' meaning a legally enforceable right to collect payments from the guarantor. By contrast, the Guidance interpreted a ''guarantee'' to include not only the foregoing, ''but also other formal arrangements that, *in view of all the facts and circumstances,* support the non-U.S. person's ability to pay or perform its swap obligations with respect to its swaps.'' [16]

The concept of a guarantee is important to our cross-border rules for swap dealers in part because a guarantee of a non-U.S. person's swap obligations by a US person can require the non-US person—or its non-US counterparty—to count the swap towards its *de minimis* swap dealer registration threshold. But when the determination of whether an entity must register with the CFTC depends on whether the entity's or its counterparty's obligations under a swap are guaranteed by a U.S. person, the meaning of the term ''guarantee'' cannot be left to a review of ''all the facts and circumstances.''

A rule in which non-US persons must try to determine, or obtain representations from non-U.S. counterparties regarding, whether the CFTC might subsequently conclude that a particular arrangement satisfies an open-ended definition of a ''guarantee'' is not a workable rule. By contrast, the definition of a ''guarantee'' in the final rules, which is based on concepts of legal recourse and a legally enforceable right to recover, is clear and workable. Some may downplay the importance of ''workability'' in Commission rulemakings, but no matter how well-intentioned a rule may be, if it is not workable, it cannot deliver on its intended purpose.

Significant Risk Subsidiaries

Some commenters objected that the definition of a ''significant risk subsidiary'' inappropriately substitutes oversight by the Board of Governors of the Federal Reserve System (the ''FRB''), and/or foreign regulatory authorities, for the Commission's regulation of derivatives market activity overseas. A significant risk subsidiary, or ''SRS,'' is a non-U.S. ''significant subsidiary'' (based on varioU.S. numerical metrics set out in the final rules) of an ultimate U.S. parent entity that has more than $50 billion in global consolidated assets. Excluded from the definition, however, are non-U.S. subsidiaries that are subject to either: (1) Consolidated supervision and regulation by the FRB as a subsidiary of a U.S. bank holding company (''BHC'') or intermediate holding company (''IHC''); or (2) capital standards and oversight by the subsidiary's home country supervisor that are consistent with Basel requirements and subject to margin requirements for uncleared swaps in a jurisdiction for which the Commission has issued a margin comparability determination. It is these exclusions that commenters have cited as a concern.

To this, there are three responses. First, as discussed above, in exercising the Commission's oversight responsibilities with respect to an SRS (which, again, is a non-U.S. subsidiary), we look to the risk that such a subsidiary poses to its ultimate parent in the United States, and thus to the U.S. financial system. It is not that we are replacing our oversight responsibilities with those of the FRB or foreign regulators. Rather, it is that we have determined that the risk presented by foreign subsidiaries consolidated with a BHC or IHC, or subject to regulation as specified in the SRS definition in their home country, is already being adequately monitored and thus does not warrant an additional layer of regulation by the CFTC.

Second, we must compare the SRS definition in the final rules to what it replaces in the Guidance: The ''conduit affiliate.'' The Guidance did not actually define a conduit affiliate, but rather described it in terms of certain ''factors.'' The most critical factor, but unfortunately also the most amorphous, was the last one, which asked whether ''the non-U.S. person in the regular course of business, engages in swaps with non-U.S. third-party(ies) for the purpose of hedging or mitigating risks faced by, or to take positions on behalf of, its U.S. affiliate(s), and enters into offsetting swaps or other arrangements with its U.S. affiliate(s) in order to transfer the risks and benefits of such swaps with third-party(ies) to its U.S. affiliates.'' [17]

As with the definition of a ''guarantee,'' I make no apologies for supporting the workable definition of an SRS in the final rules, which is based on objective and observable metrics, as compared to the ambiguous description of a conduit affiliate set forth in the Guidance. We owe the global swaps market the certainty that can only come from clarity in our rules, and the definition of an SRS in the final rules fits the bill.

Third, the record before us does not afford any basis on which to conclude that the definition of an SRS in the final rules will lead to any less robust Commission oversight of the cross-border swap activities of swap dealers than does the vague description of a conduit affiliate in the Guidance. We have no evidence that the number of non-U.S. entities that have waded through the multi-faceted conduit affiliate description in the Guidance and concluded that they were a conduit affiliate, but would conclude that they are not an SRS under the definition in the final rules, is significant—or even material. If experience going forward proves otherwise, the Commission can always amend the SRS definition accordingly. But absent such evidence, hypothetical concerns are an insufficient basis on which to reject the clear and workable SRS definition in the final rules.

ANE Transactions, Exceptions to Regulatory Requirements, and Substituted Compliance

Finally, some may see a retreat from the Guidance in the Commission's determinations: (1) Not to apply its group A, group B, or group C requirements [18] to swaps of a non-U.S. swap dealer with a non-U.S. counterparty where the non-U.S. swap dealer uses personnel or agents in the United States to arrange, negotiate, or execute the swaps (''ANE transactions''); (2) to except certain foreign-based swaps from the group B and group C requirements; and (3) to expand the availability of substituted compliance to encompass group B requirements for swaps between a U.S. branch of a non-U.S. swap dealer and certain non-U.S. counterparties. I respectfully disagree.

First, the notion that the CFTC's swap regulatory regime should apply to ANE transactions was not stated in the Commission's Guidance; rather, it was stated in a staff Advisory published after the Guidance was adopted. The Commission has never endorsed that staff view, and it has never taken effect.[19] Second, the exceptions from swap dealer requirements that apply to the swaps of non-U.S. swap dealers with non-U.S. persons, again, generally codify

[16] Guidance, 78 FR at 45320 (emphasis added).

[17] Guidance, 78 FR at 45318 n.258 and 45359.

[18] Under the final rules: (1) Group A requirements for swap dealers generally relate to the Chief Compliance Officer requirement, risk management, swap data recordkeeping, and antitrust considerations; (2) group B requirements for swap dealers generally relate to swap trading relationship documentation, portfolio reconciliation and compression, trade confirmation, and daily trading records; and (3) group C requirements for swap dealers generally relate to external business conduct rules, including voluntary initial margin segregation.

[19] Today's release acknowledges that the policy the Commission is adopting with respect to the applicability of CFTC requirements to non-U.S. swap dealers' ANE transactions differs from that taken by the SEC. But as has often been said, harmonization with the SEC, while an important goal and one that Congress supported in Dodd-Frank, should not be undertaken simply for harmonization's own sake. Here, the Commission has determined that, in light of Congress' decision to define security-based swaps as ''securities'' in Dodd-Frank, harmonization with the SEC's determination to apply its existing, pre-Dodd-Frank securities broker-dealer regulation to ANE transactions in security-based swaps is not appropriate.

exceptions that were included in the Guidance, too.

To be sure, based on input we received in the comments, the final rules include two exceptions to swap dealer regulatory requirements that were not included in the Proposal. Yet, to take one as an example, today's release explains that the ''Limited Swap Entity SRS/Guaranteed Entity Group B Exception'' is: (1) *Tailored* to placing foreign swap dealer subsidiaries of U.S. firms on the same footing as foreign branches of U.S. swap dealers; (2) *consistent* with an exception in the Guidance that was not carried forward in the Proposal;[20] and (3) *limited* in terms of the amount of swaps that can be entered into in reliance on the exception, and unavailable if the parties can rely on substituted compliance instead.

But what is critically important for the treatment of ANE transactions, the exceptions to certain regulatory requirements, and substituted compliance in the final rules is to keep in mind the scenario at issue: Although in some instances activity with respect to the swap may occur in the United States, the swaps involve non-U.S. swap dealers (or foreign branches of U.S. swap dealers) and a non-U.S. counterparty (or a foreign branch of a U.S. person) and, therefore, will also be subject to regulation in another jurisdiction. Where the regulatory interest of that other jurisdiction is paramount, the CFTC should appropriately defer, just as where the Commission's regulatory interest is paramount, we expect other foreign jurisdictions to defer to our regulation. As I stated in connection with a recent Open Meeting that also addressed cross-border issues:

[T]he Commission's historical commitment to appropriate deference to our international regulatory colleagues (which also is sometimes referred to as mutual recognition), 'is a demonstration of international comity—an expression of mutual respect for the important interests of foreign sovereigns.' This deference also reflects the shared goals of global authorities seeking to achieve the most effectively regulated markets through coordination rather than duplication.[21]

The Commission's historical commitment to mutual recognition is in keeping with principles of international comity. In reviewing the comment letters, frankly, there sometimes seems to be a sense that ''international comity'' is simply a buzzword the Commission invokes to justify what critics believe is an improper easing of its regulation of cross-border activity. I emphatically reject the notion that appropriate deference to international regulatory authorities weakens oversight or protections of our markets, market participants, or financial system. To the contrary, our reliance on international comity is deeply rooted in several sources.

First, as discussed in greater detail in the release, the Restatement (Fourth) of Foreign Relations Law of the United States counsels that even where a country has a basis for extraterritorial jurisdiction, it should not prescribe law with respect to a person or activity in another country when the exercise of such jurisdiction is unreasonable.[22] This doctrine of reasonableness is ''a principle of statutory interpretation''[23] that has been recognized in Supreme Court case law.[24]

Second, Congress in Dodd-Frank specifically directed the Commission, ''[i]n order to promote effective and consistent global regulation of swaps,'' to ''consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation . . . of swaps [and] swap entities . . .''[25] Congress recognized that global swap markets cannot function absent consistent international standards.

Third, as I have previously observed on multiple occasions, when the G–20 leaders met in Pittsburgh in the midst of the financial crisis in 2009, they, too, recognized that due to the global nature of the derivatives markets, designing a workable solution, though complicated, demands coordinated policies and cooperation.[26] To do otherwise would ignore the reality that modern markets are not bound by jurisdictional borders.

And fourth, this Commission historically has been a global leader in its commitment to applying principles of international comity, in the form of mutual recognition, in a variety of contexts. That commitment is reflected in the Commission's Part 30 rules,[27] which apply to foreign firms ''with respect to the offer and sale of foreign futures and options to U.S. customers and are designed to ensure that such products offered and sold in the U.S. are subject to regulatory safeguards comparable to those applicable to transactions entered into on designated contract markets.''[28] It also is reflected in our approach (initially through staff no-action relief, and later through registration after Dodd-Frank) to foreign boards of trade (''FBOTs'') offering US participants ''direct access'' to enter trades directly into the FBOT's order entry and trade matching systems.[29] And just recently, it was reflected in the Commission's proposal to amend Rule 3.10(c)(3) to permit non-US commodity pool operators to claim exemption from CFTC registration for offshore commodity pools with no US participants on a pool-by-pool basis.[30]

When the Commission issued the Guidance in 2013, only a few derivatives reforms had been adopted in a few other jurisdictions. How things have changed since then. Many of our fellow regulators in the world's major financial centers have implemented reforms governing the conduct of swap dealers commensurate to our own, and extensive strides have been made (and continue to be made) towards international harmonization—thereby aligning our regulatory principles, just as the G–20 envisioned. As a result, most swaps involving non-U.S. counterparties today are expected to be subject to foreign regulatory requirements similar to the Commission's own, unlike at the time the Guidance was adopted.[31] Further, our deference to the comprehensive swap regulation of our international colleagues has been demonstrated by the fact that since the Guidance was issued, the CFTC has issued 11 comparability determinations regarding the regulation of swap dealers in the European Union, Canada, Japan, Australia, Hong Kong, and Switzerland.

Thus, regulation of global swap markets that imposes overlapping and duplicative requirements on swap dealers and their cross-border activities by multiple regulators is inconsistent with: (1) Principles of statutory interpretation; (2) Congress' direction to the Commission; (3) the vision of the G–20 Leaders at the Pittsburgh Summit; and (4) the Commission's own longstanding commitment to international comity through mutual recognition of foreign regulatory regimes. In a word: It is not workable.

[20] The release explains that under the Guidance, a non-U.S. person that was guaranteed by a U.S. person or a conduit affiliate would not have been expected to comply with group B requirements when transacting with a non-U.S. counterparty that also was not guaranteed by a U.S. person or a conduit affiliate.

[21] *See* Commissioner Stump Part 3 Statement, n.15, *supra* (footnote omitted).

[22] Restatement (Fourth) section 405 cmt. A (Westlaw 2018).

[23] *Id.*

[24] *See F. Hoffman-LaRoche, Ltd.* v. *Empagran S.A.,* 542 U.S. 155, 164 (2004) (statutes should be construed to ''avoid unreasonable interference with the sovereign authority of other nations.'').

[25] Dodd-Frank, Section 752(a).

[26] *See* Leaders' Statement from the 2009 G–20 Summit in Pittsburgh, Pa. (''G–20 Pittsburgh Leaders' Statement'') at 7 (Sept. 24–25, 2009) (''We are committed to take action at the national and international level to raise standards together so that our national authorities implement global standards consistently in a way that ensures a level playing field and avoids fragmentation of markets, protectionism, and regulatory arbitrage''), *available at https://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf.*

[27] 17 CFR part 30.

[28] Foreign Futures and Options Transactions, 85 FR 15359, 15360 (March 18, 2020).

[29] *See* Statement of Commissioner Dawn D. Stump Regarding Foreign Board of Trade Registration Applications of Euronext Amsterdam, Euronext Paris, and European Energy Exchange (November 5, 2019), available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/stumpstatement110519.*

[30] Exemption From Registration for Certain Foreign Persons Acting as Commodity Pool Operators of Offshore Commodity Pools, 85 FR 35820 (June 12, 2020); *see also* Commissioner Stump Part 3 Statement, n.15, *supra.*

[31] As recounted in the release, CEA Section 2(i) has its origins in an amendment that Rep. Spencer Bachus offered during the House Financial Services Committee markup on October 14, 2009, that would have restricted the Commission's jurisdiction over swaps between non-U.S. resident persons. Chairman Frank opposed the amendment, noting that there may well be cases where non-U.S. residents are engaging in transactions that have an effect on the United States and that are insufficiently regulated internationally and that he would not want to prevent U.S. regulators from stepping in. Chairman Frank expressed his commitment to work with Rep. Bachus going forward, Rep. Bachus withdrew the amendment, and eventually Section 2(i) was included in Dodd-Frank. *See* H. Fin. Serv. Comm. Mark Up on Discussion Draft of the Over-the-Counter Derivatives Markets Act of 2009, 111th Cong., 1st Sess. (Oct. 14, 2009) (statements of Rep. Bachus and Rep. Frank). For the reasons discussed in text, the prospect of swaps between non-U.S. counterparties being insufficiently regulated internationally is far less today than it was when the extraterritoriality of the CFTC's jurisdiction over swaps was being debated.

Conclusion

In conclusion, I support codifying our prior cross-border Guidance into enforceable rules. I believe that the final rules before us today are clear, sensible, and workable, and that they appropriately apply the Commission's regulations to the cross-border activities of swap dealers. They improve upon the Guidance based on our experience in administering the Dodd-Frank swap regulatory regime over the past several years, and they recognize the current state of global regulation of globally interconnected derivatives markets by carrying on this agency's established tradition of mutual recognition and substituted compliance.

I therefore support the final cross-border rules for swap dealers before us today. I want to very much thank the staff of the Division of Swap Dealer and Intermediary Oversight, the General Counsel's Office, and the Chief Economist's Office for their efforts in preparing this rulemaking. I am particularly appreciative of the time that the staff devoted to answering our diverse questions—always in a thoughtful and comprehensive manner—and reviewing and addressing the various comments and requests from me and my team.

Appendix 6—Dissenting Statement of Commissioner Dan M. Berkovitz

Introduction

I dissent from today's final cross-border swap rulemaking (the ''Final Rule''). As described by the Chairman, this Final Rule will ''pare[] back our extraterritorial application of our swap dealer regime.'' [1] Over the past seven years, the current cross-border regime has helped protect the U.S. financial system from risky overseas swap activity. The Commission should not be paring back these protections for the American financial system, particularly now, during a global pandemic.

The Final Rule will permit U.S. swap dealers to book their swaps with non-U.S. persons in offshore affiliates, thereby avoiding the CFTC's swap regulations, even when they conduct those swap activities from within the United States and the U.S. parent retains the risks from those swap activities. The structure of the Final Rule practically invites multinational U.S. banks and hedge funds to book their swaps in offshore affiliates to avoid our swap dealer regulations. This will permit risks to flow back into the United States with none of the intended regulatory protections.

The Commission defends its retreat by citing principles of international comity and asserting that compliance with the laws of another jurisdiction in lieu of the CFTC's requirements will be permitted only when the CFTC finds that the laws of the other jurisdiction are ''comparable'' to those of the CFTC. The Final Rule, however, establishes a weak and vague standard for determining when the swap regulations of another jurisdiction are comparable. Further, the Final Rule even permits substituted compliance where the swap activity occurs within the United States—such as for swaps between a U.S. branch of a non-U.S. swap dealer and another non-U.S. person, even if those swaps are negotiated and booked in the United States. The Commission is not permitted to defer to regulators in other jurisdictions when the swap activity is conducted within the United States, nor should it do so even if such deference were permitted.

As I noted in my dissent on the proposed rule, experience has taught us that while finance may be global, global financial rescues are American. We should not loosely outsource the protection of the U.S. financial system and American taxpayers to foreign regulators that are unaccountable to the American people.

Less Regulation of U.S. Persons Conducting Swap Activities Outside the U.S.

In the Final Rule, the Commission acknowledges that cross-border swaps activities can have a ''direct and significant'' connection with activities in, or effect on, U.S. commerce. The Final Rule, however, removes several key protections in the 2013 Cross-Border Guidance (''Guidance'') [2] that mitigated the risks arising from such cross-border activities.[3] The Final Rule narrows the definition of ''guarantee'' in a legalistic manner, permitting banks to craft financing arrangements for their overseas swap activities that bring risks back into the U.S. parent organization without triggering the application of Dodd-Frank requirements for those activities. The Final Rule also discards the Guidance's firewalls that were designed to prevent banks from evading Dodd-Frank requirements by using foreign affiliates as the front office for swaps with non-U.S. persons while bringing the risk from those swaps back to the U.S. home office through back-to-back internal swaps (''affiliate conduits'').

The Final Rule creates a new category of entities—the SRS—supposedly to capture the risks arising from the swap activities of very large foreign affiliates of U.S. firms. But the Commission admits that this new category likely will include ''few, if any'' entities.[4] Most likely, therefore, the SRS construct will provide no protections to the financial system from the swap activities of overseas affiliates of U.S. entities that bring risks to their U.S. parents and to the U.S. financial system. Each of these significant deficiencies is discussed in greater detail below.

Swap activity outside the U.S. guaranteed by a U.S. Person. The Guidance provided that when a swap of a non-U.S. person is guaranteed by a U.S. person, then the Dodd-Frank requirements regarding swap dealer registration and many of the attendant swap dealer regulations would apply to that non-U.S. person in the same manner as they would apply to a U.S. person. This is because a swap conducted by a non-U.S. person guaranteed by a U.S. person poses essentially the same risks to the U.S. financial system as a swap conducted by a U.S. person.[5] The Guidance adopted a functional rather than literal approach to the term ''guarantee'':

> The Commission also is affirming that, for purposes of this Guidance, the Commission would interpret the term ''guarantee'' generally to include not only traditional guarantees of payment or performance of the related swaps, but also other formal arrangements that, in view of all the facts and circumstances, support the non-U.S. person's ability to pay or perform its swap obligations with respect to its swaps. The Commission believes that it is necessary to interpret the term ''guarantee'' to include the different financial arrangements and structures that transfer risk directly back to the United States. In this regard, it is the substance, rather than the form, of the arrangement that determines whether the arrangement should be considered a guarantee for purposes of the application of section 2(i).[6]

The Final Rule, however, adopts a narrow, legalistic definition of guarantee: ''Guarantee means an arrangement pursuant to which one party to a swap has rights of recourse against a guarantor, with respect to its counterparty's obligations under the swap.'' [7] The Commission recognizes that this definition is ''narrower'' than the definition in the Guidance, and that this narrower definition could result in increased risk to the U.S. financial system.[8] The Commission further acknowledges that this narrower definition ''could lead to certain entities counting fewer

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[1] Kadhim Shubber, Financial Times, *U.S. regulator investigates oil fund disclosures* (July 15, 2020), available at *https://www.ft.com/content/1e689137-2d1f-4393-a18f-fe0da02141cc.*

[2] Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations, 78 FR 45292, 45298–45301 (July 26, 2013).

[3] The preamble to the final rule observes (Sec. I.C.):

> In this sense, a global financial enterprise effectively operates as a single business, with a highly integrated network of business lines and services conducted through various branches or affiliated legal entities that are under the control of the parent entity. [footnote omitted]. Branches and affiliates in a global financial enterprise are highly interdependent, with separate entities in the group providing financial or credit support to each other, such as in the form of a guarantee or the ability to transfer risk through inter-affiliate trades or other offsetting transactions. Even in the absence of an explicit arrangement or guarantee, a parent entity may, for reputational or other reasons, choose to assume the risk incurred by its affiliates, branches, or offices located overseas. Swaps are also traded by an entity in one jurisdiction, but booked and risk-managed by an affiliate in another jurisdiction. The Final Rule recognizes that these and similar arrangements among global financial enterprises create channels through which swap-related risks can have a direct and significant connection with activities in, or effect on, commerce of the United States.

[4] Final Rule release, Sec. X.C.3.

[5] ''The Commission believes that swap activities outside the U.S. that are guaranteed by U.S. persons would generally have a direct and significant connection with activities in, or effect on, U.S. commerce in a similar manner as the underlying swap would generally have a direct and significant connection with activities in, and effect on, U.S. commerce if the guaranteed counterparty to the underlying swap were a U.S. person.'' Cross-Border Guidance, 78 FR at 45319.

[6] *Id.* at 45320 (footnotes omitted).

[7] Final Rule release, Section 23.23(a)(9).

[8] The Commission states that arrangements that would meet the broader definition in the Guidance, but are not within the narrower scope of the Final Rule, ''transfer risk directly back to the U.S. financial system, with possible adverse effects, in a manner similar to a guarantee with direct recourse to a U.S. person.'' Final Rule release, Sec. II.C.3.

swaps towards their de minimis threshold or qualify additional counterparties for exceptions to certain regulatory requirements as compared to the definition in the Guidance.'' [9]

The Commission asserts, however, that the narrower definition is ''more workable'' because it is consistent with the definition of guarantee in the Cross-Border Margin Rule, and therefore will not require an ''independent assessment.'' [10] The Commission presents no evidence, however, as to why the current definition, which has now been in place for seven years, is not ''workable,'' or why multinational financial institutions that trade hundreds of billions, and even trillions, of dollars of swaps on a daily basis are not capable of determining whether their overseas affiliates are guaranteed by a U.S. person. A global financial institution that cannot readily determine or represent whether or not the risks from its overseas swaps are guaranteed by one of its U.S. entities should not be a global financial institution.

Affiliate conduits. The Guidance also applied the Dodd-Frank swap dealer registration requirements, and many of the attendant swap dealer regulations, to the swap activities of ''affiliate conduits'' [11] of U.S. persons in the same manner as it applies to U.S. persons. Under the Guidance, a key factor in determining whether a non-U.S. person would be considered to be an affiliate conduit of a U.S. person is whether the non-U.S. person regularly enters into swaps with non-U.S. counterparties and then enters into ''offsetting swaps or other arrangements with its U.S. affiliate(s) in order to transfer the risks and benefits of such swaps with third parties to its U.S. affiliates.'' [12]

The affiliate conduit provisions in the Guidance were designed to prevent U.S. entities from booking those swaps in their non-U.S. affiliates to escape the CFTC's Dodd-Frank requirements that would otherwise apply to the entity's swap activity in the United States. The risks and benefits of those swaps booked offshore could then be transferred back to the U.S. with back-to-back internal swaps between the U.S. parent and its non-U.S. affiliate. Ultimately, risk from the swap would reside on the books of the U.S. entity. Through this back-to-back process, the U.S. entity could still conduct the swap activity, and bear the risk of the swaps, yet would avoid the application of CFTC requirements that would apply had the swap been booked directly in the U.S. entity.

The Final Rule does not include any comparable provisions to prevent the use of affiliate conduits to avoid CFTC regulation. This is an invitation to abuse and to risk for the U.S. financial system.

Significant risk subsidiary (SRS). The Final Rule adopts a new construct—the ''significant risk subsidiary''—to supposedly encompass overseas affiliates of U.S. entities whose swap activities pose significant risks to the U.S. financial system. An SRS is defined as any non-U.S. ''significant subsidiary'' of an ultimate U.S. parent entity where that ultimate parent has more than $50 billion in global consolidated assets. An entity is a ''significant subsidiary'' if it has a sufficient size relative to its parent, measured in terms of percentage of either revenue, equity capital, or total assets.[13] However, the definition then excludes non-U.S. subsidiaries that are either (i) prudentially regulated by the Federal Reserve; or (ii) prudentially regulated by the entity's home country prudential regulator whose regulations are consistent with the Basel Committee's capital standards, and subject to comparable margin requirements for uncleared swaps in its home country. An entity that survives the gantlet of thresholds and exclusions to be considered an SRS would then be subject to the same registration requirements as a U.S. person, and many of the same regulatory requirements that apply to U.S. swap dealers. That outcome, however, is very unlikely. The threshold criteria to be a ''significant subsidiary'' are high, and because entities that meet these high thresholds are typically affiliated with prudentially-regulated banks, it is likely they will be excluded from the SRS definition. It therefore is improbable that any entities will fall into the SRS category. The Cost-Benefit Considerations in the notice of proposed rulemaking for the Final Rule concede that ''few, if any'' entities would fall within its ambit.[14]

Furthermore, the criteria apply to each subsidiary separately. If an institution has a subsidiary that is approaching the high thresholds set in the Final Rule, it can incorporate another non-U.S. subsidiary and conduct swap dealing activity out of that entity to avoid SRS designation for any of its subsidiaries.

One commenter noted that the qualifications only indirectly address the significance of the subsidiary and suggested the test be modified to assess the extent to which swap risk is accepted by a non-U.S. subsidiary or transferred back to the subsidiary's U.S. affiliates.[15] The Commission characterized the suggested test as an activity-based test and rejected the commenter's proposed fix. On the other hand, when other commenters noted that subsidiaries that do not engage in any swap dealing activity would potentially be captured by the SRS qualifications—because the qualifications have *nothing to do with swaps*—the Commission modified the Final Rule with an activity-based end-user test to exempt those entities from the SRS category.

Under the Final Rule, a significant subsidiary that is regulated by U.S. or foreign banking regulators is *excluded* from the SRS category. ''The Commission is excluding these entities from the definition of SRS, in large part, because the swaps entered into by such entities are already subject to significant regulation, either by the Federal Reserve Board or by the entity's home country.'' [16]

Here the Commission forgets the lessons of the 2008 financial crisis and ignores the mandate of Congress. Following the financial crisis—and as a result of the lessons learned during the crisis—Congress subjected the swaps markets to *both* prudential and market regulation. The Commodity Futures Modernization Act of 2000, which spectacularly failed to prevent the build-up of catastrophic systemic risks within the financial system leading to the 2008 financial crisis, was based on the premise that market regulation is unnecessary to protect against systemic risks for financial entities that are subject to prudential regulation.[17] Events taught us, however, that prudential regulation alone was insufficient to prevent the build-up of those risks to the financial system. Following the crisis, Congress mandated both prudential regulation and market regulation for banks conducting swap activities. The safeguards and protections to the financial system afforded under Title VII of the Dodd-Frank Act were to be applied regardless of the extent of prudential regulation. The prudential regulation in a non-U.S. jurisdiction of an affiliate of a U.S. swap dealer whose swaps risks are transferred back into the U.S. is not an adequate substitute for the protections mandated by Title VII of the Dodd-Frank Act.

The Commission does not dispute that the Final Rule will allow affiliates currently subjected to the Guidance provisions regarding guarantees and affiliate conduits affiliates to operate free of CFTC swap regulations. The Commission also acknowledges that the activities of these entities may pose risks to the U.S. financial system.[18] Not only will the Final Rule permit

[9] *Id.*

[10] *Id.*

[11] The term ''affiliate conduit'' and ''conduit affiliate'' are used interchangeably. *See, e.g.,* Cross-Border Guidance, 78 FR at 45319.

[12] The Commission explained, ''the Commission believes that swap activities outside the United States of an affiliate conduit would generally have a direct and significant connection with activities in, or effect on, U.S. commerce in a similar manner as would be the case if the affiliate conduit's U.S. affiliates entered into the swaps directly.'' *Id.*

[13] The Final Rule release asserts that the criteria for qualifying as a ''significant subsidiary'' are risk-based. The relative financial measures of revenue, equity capital, and total assets, however, are not related to the risks presented by the subsidiary's swap activity. These criteria have nothing at all to do with swaps and in no way a measure or reflect the risks posed by the subsidiary's swap activities.

[14] ''Of the 61 non-U.S. SDs that were provisionally registered with the Commission in June 2020, the Commission believes that few, if any, will be classified as SRSs pursuant to the Final Rule.'' Final Rule release, Sec. X.C.3.

[15] Better Markets, Comment Letter, Cross-Border Application of the Registration Thresholds and Certain Requirements Applicable to Swap Dealers and Major Swap Participants, at 17 (Mar. 9, 2020); available at *https://comments.cftc.gov/Handlers/PdfHandler.ashx?id=29136.*

[16] Final Rule release, Sec. II.D.3.iv.

[17] For a more detailed discussion of the financial firm failures involving cross border activity and related U.S. government and bail outs, see my dissenting statement to the Proposed Cross-border swap regulations (Dec. 18, 2019), available at *https://www.cftc.gov/PressRoom/SpeechesTestimony/berkovitzstatement121819b.*

[18] ''The Commission is aware that many other types of financial arrangements or support, other than a guarantee as defined in the Final Rule, may be provided by a U.S. person to a non-U.S. person (*e.g.,* keepwells and liquidity puts, certain types of indemnity agreements, master trust agreements, liability or loss transfer or sharing agreements). The Commission understands that these other financial arrangements or support transfer risk directly back to the U.S. financial system, with possible adverse effects, in a manner similar to a guarantee with a

risks to flow into the U.S., but it will provide an incentive for U.S. banks to move their swap activities into these foreign affiliates, where they can conduct the same activities but be free from the CFTC's regulations.

Less Regulation of Swap Activity in the U.S.

ANE Swaps. In 2013, the CFTC issued a Staff Advisory addressing the applicability of the ''Transaction-Level Requirements'' to non-U.S. swap dealers that use persons in the U.S. to facilitate swap transactions with other non-U.S. persons. The CFTC staff observed that ''persons regularly arranging, negotiating, or executing swaps for or on behalf of an SD [swap dealer] are performing core, front-office activities of that SD's dealing business,'' and declared that ''the Commission has a strong supervisory interest in swap dealing activities that occur within the United States, regardless of the status of the counterparties.'' [19] The CFTC staff advised that a non-U.S. swap dealer ''regularly using personnel or agents located in the U.S. to arrange, negotiate, or execute [''ANE''] a swap with a non-U.S. person generally would be required to comply with the Transaction-Level Requirements.'' [20]

The Staff Advisory prompted an outcry from non-U.S. swap dealers, including wholly-owned non-U.S. affiliates of U.S. financial institutions, who objected to the CFTC's imposition of its clearing, trade execution, reporting, and business conduct standards on their swaps with other non-U.S. persons. Non-U.S. dealers argued that the risks from these swap activities resided primarily in the home country, and warned that they may remove their swap dealing business from the U.S. if these requirements applied. Shortly thereafter, the CFTC staff provided no-action relief from the application of the Staff Advisory,[21] and the Commission issued a Request for Comment on whether the Commission should adopt the Staff Advisory, in whole or in part.[22]

The Final Rule discards the ANE concept entirely. ''ANE transactions will not be considered a relevant factor for purposes of applying the Final Rule.'' [23]

The ability of non-U.S. persons to use personnel within the U.S., without limitation, to conduct their swap activities with other non-U.S. persons without CFTC regulation or oversight could have a variety of detrimental consequences. Foremost among these is the possibility, perhaps even likelihood, that U.S. swap dealers will move the booking of their swaps with non-U.S. persons (including non-U.S. affiliates of other U.S. firms) into their own non-U.S. affiliates, while maintaining the U.S. location of the personnel conducting the swap business, in order to avoid the application of the Dodd-Frank requirements to those transactions. In fact, Citadel noted in its comments on the proposed rule that this may be happening already. Citadel stated that ''market transparency in EUR interest rate swaps for U.S. investors has been greatly reduced based on data showing that, following issuance of the ANE No-Action Relief, interdealer trading activity in EUR interest rate swaps began to be booked almost exclusively to non-U.S. entities, a fact pattern that Citadel believes is 'consistent with (although not direct proof of) swap dealers strategically choosing the location of the desk executing a particular trade in order to avoid trading in a more transparent and competitive setting.' '' [24]

If more than one U.S. swap dealer were to employ this strategy, the result could be that swap activity between two U.S. swap dealers that currently takes place within the U.S. and is fully subject to the CFTC's swap regulations might then be booked in two non-U.S. affiliates outside the United States. So long as the U.S. parents do not provide explicit guarantees for the swaps of the subsidiaries,[25] the trading between these subsidiaries would not count toward the dealer registration threshold. Furthermore, even if one of those non-U.S. entities were a registered swap dealer, the trading would not be subject to any CFTC transaction-level requirements, even though the risk from those transactions is ultimately borne by the U.S. parent through consolidated accounting, and U.S. personnel would be negotiating those transactions.[26]

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direct recourse to a U.S. person.'' Final Rule release, Sec.II.C.3. See also Final Rule release, Sec. II.D.3 (recognition that conduit affiliate structures may present significant risks to the U.S. financial system but determination not to apply de minimis registration threshold to a non-U.S. affiliates that is not an SRS).

[19] CFTC Staff Advisory 13–69, Division of Swap Dealer and Intermediary Oversight Advisory, Applicability of Transaction Level Requirements to Activity in the United States (Nov. 14, 2013), available at *https://www.cftc.gov/csl/13-69/download.*

[20] *Id.*

[21] CFTC No-Action Letter No. 13–71, Certain Transaction-Level Requirements for Non-U.S. Swap Dealers (Nov. 26, 2013), available at *https://www.cftc.gov/csl/13-71/download.* This no-action relief has been extended multiple times and will continue in effect until the Final Rule becomes effective. Concurrent with the issuance of the Final Rule, the CFTC staff is extending this no-action relief for transaction-level requirements not addressed by the Final Rule (which includes requirements relating to clearing, trade-execution, and real-time public reporting). At the same time, the staff is withdrawing the 2013 Staff Advisory as it applies to all transaction-level requirements, including requirements not addressed in the Final Rule. In conjunction with the Commission's consideration of the Final Rule, both of these staff actions were presented to the Commission in a single package under the ''Absent Objection'' process, with any objections due the day before the Commission is scheduled to vote on the Final Rule. Although I would support the extension of this no-action relief for such transactions not covered by this rulemaking, were it issued separately, I cannot support, in conjunction with this rulemaking, the withdrawal of the ANE advisory for transactions not covered by the Final Rule. The withdrawal of the Staff Advisory for transactions not covered by the rulemaking is being taken in response to selected comments received as part of the rulemaking, yet the public was not afforded notice and opportunity for comment as to the manner in which the Commission should address transaction-level requirements not within the scope of the rulemaking. It would have been just as workable for market participants to provide the no-action relief while maintaining the Staff Advisory. Accordingly, I have objected to the ''Absent Objection'' package presented to the Commission that included both the withdrawal of the Staff Advisory and the extension of no-action relief for transactions not covered by the Final Rule.

[22] Request for Comment on Application of Commission Regulations to Swaps Between Non-U.S. Swap Dealers and Non-U.S. Counterparties Involving Personnel or Agents of the Non-U.S. Swap Dealers Located in the United States, 79 FR 1347 (Jan. 8, 2014).

[23] Final Rule release, Sec. V.C. The Securities and Exchange Commission (''SEC'') requires a non-U.S. person to include ANE transactions in determining whether the amount of its swap dealing activity exceeds the de minimis threshold for registration. Cross-Border Application of Certain Security-Based Swap Requirements, 85 FR 6270, 6272 (Feb. 4, 2020), available at *https://www.federalregister.gov/documents/2020/02/04/2019-27760/cross-border-application-of-certain-security-based-swap-requirements.* The preamble to the Final Rule includes many statements regarding the importance of ''harmonization'' with the SEC rules. However, on this issue, which imposes a more stringent result for potential swap dealers, the Commission has decided *not* to harmonize with the SEC.

[24] Final Rule release, Sec. V.C. In support of this assertion, Citadel cites Evangelos Benos, Richard Payne and Michalis Vasios, Bank of England Staff Working Paper (No. 580), Centralized trading, transparency and interest rate swap market liquidity: Evidence from the implementation of the Dodd-Frank Act (May 2018), available at: *https://www.bankofengland.co.uk/-/media/boe/files/working-paper/2018/centralized-trading-transparency-and-interest-rate-swap-market-liquidity-update.* In addition to the language quoted by Citadel, this study concluded:

Additionally, we find that, for the EUR-denominated swap market, the bulk of interdealer trading previously executed between U.S. and non-U.S. trading desks is now largely executed by the non-U.S. (mostly European) trading desks of the same institutions (*i.e.* banks have shifted inter-dealer trading of their EUR swap positions from their U.S. desks to their European desks). We interpret this as an indication that swap dealers wish to avoid being captured by the SEF trading mandate and the associated impartial access requirements. Migrating the EUR inter-dealer volume off-SEFs enables dealers to choose who to trade with and (more importantly) who not to trade with. This might allow them to erect barriers to potential entrants to the dealing community. Thus this fragmentation of the global market may be interpreted as dealers trying to retain market power, where possible. Importantly, we find no evidence that customers in EUR swap markets try to avoid SEF trading and the improved liquidity it delivers.

Id. at 31–32.

[25] Even in the absence of an explicit guarantee or other financial support, there is likely an expectation that the U.S. parent will ensure the subsidiary has sufficient funds to pay its swap obligations. The U.S. parent has substantial reputation risk if its subsidiaries start defaulting on their swaps. The expansive definition of ''guarantee'' in the Guidance is perhaps one reason that U.S. banks that withdrew the explicit guarantees provided their affiliates have not yet attempted to withdraw their swap dealer registration. Further regulatory uncertainty about the viability of de-registering may have arisen from the cross-border rule proposed by the Commission in 2016 that would have treated non-U.S. affiliates that were consolidated subsidiaries of U.S. persons as U.S. persons.

[26] This strategy would be less effective if either of the non-U.S. affiliates were an SRS. However, as described above, it is likely that ''few, if any,'' non-U.S. affiliates will be captured within this definition particularly affiliates of prudentially regulated banks, which are excepted out of the definition altogether.

U.S. banks already conduct a significant amount of inter-bank business through their non-U.S. affiliates. Data from swap data repositories shows that U.S. bank swap dealers commonly book swaps with each other through their respective non-U.S. subsidiaries. For a recent one-year period, the data shows that a number of U.S. banks booked more than 10 percent—and in some cases close to 50 percent—of the reported notional amount of swaps across their entire bank-to-bank swaps books through non-U.S. subsidiaries. In other words, a number of U.S. banks are already booking material amounts of swaps with each other through their non-U.S. wholly-owned consolidated subsidiaries.

Non-U.S. banks conducting swap activity in the U.S. The Final Rule reverses the position taken by the Commission in the proposed rule that would have prevented a U.S. branch of a non-U.S. swap entity from obtaining substituted compliance for various transactional requirements for swaps with non-U.S. swap entities that are booked in the U.S. branch.[27] The cross-border notice of proposed rulemaking upon which the Final Rule is based (''2019 Proposal'') would have permitted substituted compliance only for the foreign-based swaps of a non-U.S. swap entity. Both under the 2019 Proposal and the Final Rule, a swap conducted by a non-U.S. swap entity through a U.S. branch would not be considered a ''foreign-based swap.''

Sensibly, under the 2019 Proposal, substituted compliance would be available only for foreign-based swaps. As the Commission explained in the 2019 Proposal, ''[t]he Commission preliminarily believes that the requirements listed in the proposed definitions are appropriate to identify swaps of a non-U.S. banking organization operating through a foreign branch in the United States that should remain subject to Commission requirements. . . .''[28]

Although the Commission repeats nearly verbatim the rationale articulated in the 2019 Proposal for applying CFTC regulations without substituted compliance to transactions booked in the United States, conducted in the United States, and within an organization regulated under the laws of the United States, the Final Rule now excludes swaps booked in a U.S. branch of a non-U.S. swap entity from this general principle, and permits it to obtain substituted compliance for its transactions with non-U.S. persons.[29]

The Commission has no authority to grant substituted compliance for transactions occurring within the United States. The ability of the Commission to consider international comity in determining whether to apply CFTC regulations or permit substituted compliance with the laws of a foreign regulator only applies with respect to activities outside the United States. The Final Rule defines a ''foreign-based swap'' in a manner that does not include swaps booked in the U.S. branch of a non-U.S. swap entity. The fact that one of the counterparties to a transaction is owned by a non-U.S. entity does not transform activity conducted by that entity within the United States into foreign activity. Thus, the Final Rule not only retreats from the application of U.S. law to transactions that are arranged, negotiated, and executed in the United States, it even retreats from the application of U.S. law to transactions that are booked in the United States. This is not in accordance with either Section 2(i) of the Commodity Exchange Act (''CEA''), which limits the application of the swaps provisions of the CEA only with respect to activities outside the United States, or with the principles of international comity, which the Commission recognizes only applies with respect to activity occurring in another jurisdiction.

Weakening the Standards for Substituted Compliance

I agree with the Commission's interpretation of CEA Section 2(i) that international comity is an important consideration in determining the extent to which the CEA and the CFTC's swap regulations should apply to cross-border swap activity occurring in another jurisdiction. I have voted for every substituted compliance determination presented to the Commission during my tenure under the standards adopted in the Guidance.

The standards established in the Final Rule for substituted compliance determinations, however, depart significantly from the current standards. The Final Rule creates a lesser standard that permits a finding of comparability if the Commission determines that ''some or all of the relevant foreign jurisdiction's standards are comparable . . . or would result in comparable outcomes . . . .''[30] Under the Guidance, however, the Commission must also find that the regulations of the other jurisdiction are as ''comprehensive'' as the Commission's regulations. Furthermore, the Final Rule permits the Commission to consider any factors it ''determines are appropriate, which *may* include''[31] any of four factors listed in the Final Rule. This ''standard for review'' is not a standard at all. It permits the Commission to withdraw the cross-border application of its regulations regardless of the robustness of the other jurisdiction's regulatory regime, for whatever reasons the Commission chooses. In the absence of more rigorous, objective criteria, it will be very difficult for the Commission to deny requests from other jurisdictions or market participants for comparability determinations.

Conclusion

The Final Rule is a significant retreat from the robust yet balanced cross-border framework presented in the Guidance. The current framework has worked well to both protect the U.S. financial system from systemic risks arising from swap activities outside the U.S. and recognize the interests of other nations in regulating conduct within their own borders. The Final Rule destroys this balance.

I cannot support this abdication of responsibility to protect the U.S. financial markets and the American taxpayer.

[FR Doc. 2020–16489 Filed 9–11–20; 8:45 am]

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[27] 2019 Proposal, rule text, Sec. 23.23(e)(3), 85 FR 952, 1004.

[28] 2019 Proposal, 85 FR 952, 968.

[29] The Commission's adoption of the opposite of what was proposed also presents significant notice and comment issues under the Administrative Procedure Act. *See Environmental Integrity Project* v. *EPA,* 425 F.3d 992, 998 (''Whatever a ''logical outgrowth'' of this proposal may include, it certainly does not include the Agency's decision to repudiate its proposed interpretation and adopt its inverse.''); *Chocolate Mfrs. Ass'n* v. *Block,* 755 F.2d 1098, 1104 (''An agency, however, does not have carte blanche to establish a rule contrary to its original proposal simply because it receives suggestions to alter it during the comment period.'').

[30] Final Rule, rule text, section 23.23(g)(4).

[31] *Id.*

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Part IV

Environmental Protection Agency

40 CFR Part 60

Oil and Natural Gas Sector: Emission Standards for New, Reconstructed, and Modified Sources Review; Final Rule

ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 60

[EPA–HQ–OAR–2017–0757; FRL–10013–44–OAR]

RIN 2060–AT90

Oil and Natural Gas Sector: Emission Standards for New, Reconstructed, and Modified Sources Review

AGENCY: Environmental Protection Agency (EPA).

ACTION: Final rule.

SUMMARY: This action finalizes amendments to the oil and natural gas new source performance standards (NSPS) promulgated in 2012 and 2016. These amendments remove sources in the transmission and storage segment from the source category, rescind the NSPS (including both the volatile organic compounds (VOC) and methane requirements) applicable to those sources, and separately rescinds the methane-specific requirements of the NSPS applicable to sources in the production and processing segments. Furthermore, the U.S. Environmental Protection Agency (EPA) adopts an interpretation of Clean Air Act (CAA) section 111 under which the EPA, as a predicate to promulgating NSPS for certain air pollutants, must determine that the pertinent pollutant causes or contributes significantly to dangerous air pollution.

DATES: This final rule is effective on September 14, 2020.

ADDRESSES: The EPA established a docket for this action under Docket ID No. EPA–HQ–OAR–2017–0757. All documents in the docket are listed on the *https://www.regulations.gov/* website. Although listed, some information is not publicly available, *e.g.,* Confidential Business Information or other information whose disclosure is restricted by statute. Certain other material, such as copyrighted material, is not placed on the internet and will be publicly available only in hard copy form. Publicly available docket materials are available electronically through *https://www.regulations.gov/.* Out of an abundance of caution for members of the public and our staff, the EPA Docket Center and Reading Room are closed to the public, with limited exceptions, to reduce the risk of transmitting COVID–19. Our Docket Center staff will continue to provide remote customer service via email, phone, and webform. For further information and updates on EPA Docket Center services, please visit us online at *https://www.epa.gov/dockets.* The EPA continues to carefully and continuously monitor information from the Center for Disease Control, local area health departments, and our Federal partners so that we can respond rapidly as conditions change regarding COVID–19.

FOR FURTHER INFORMATION CONTACT: For questions about this final action, contact Ms. Amy Hambrick, Sector Policies and Programs Division (E143–05), Office of Air Quality Planning and Standards, U.S. Environmental Protection Agency, Research Triangle Park, North Carolina 27711; telephone number: (919) 541–0964; fax number: (919) 541–0516; and email address: *hambrick.amy@epa.gov.*

SUPPLEMENTARY INFORMATION: *Preamble acronyms and abbreviations.* We use multiple acronyms and terms in this preamble. While this list may not be exhaustive, to ease the reading of this preamble and for reference purposes, the EPA defines the following terms and acronyms here:

AEO Annual Energy Outlook
APA Administrative Procedure Act
BSER best system of emission reduction
CAA Clean Air Act
CFR Code of Federal Regulations
CH_4 methane
CO carbon monoxide
CO_2 carbon dioxide
CO_2 Eq. carbon dioxide equivalent
EAV equivalent annualized value
EG Emission Guidelines
EGU Electricity Generating Units
EIA U.S. Energy Information Administration
EPA Environmental Protection Agency
GHG greenhouse gases
GHGI greenhouse gas inventory
GHGRP Greenhouse Gas Reporting Program
HAP hazardous air pollutant(s)
H_2S hydrogen sulfide
ICR Information Collection Request
IR infrared
kt kilotons
MMT million metric tons
NAAQS National Ambient Air Quality Standards
NAICS North American Industry Classification System
NEI National Emissions Inventory
NEMS National Energy Modeling System
NO_X nitrogen oxides
NSPS new source performance standards
NTTAA National Technology Transfer and Advancement Act
OGI optical gas imaging
OMB Office of Management and Budget
PM particulate matter
$PM_{2.5}$ PM with a diameter of 2.5 micrometers or less
PM_{10} PM with a diameter of 10 micrometers or less
PRA Paperwork Reduction Act
PV present value
RFA Regulatory Flexibility Act
RIA Regulatory Impact Analysis
SC-CH_4 social cost of methane
SCF significant contribution finding
scfh standard cubic feet per hour
SIP state implementation plan
SO_2 sulfur dioxide
tpy tons per year
the Court United States Court of Appeals for the District of Columbia Circuit
TSD technical support document
UMRA Unfunded Mandates Reform Act
U.S. United States
VOC volatile organic compounds

Organization of this document. The information presented in this preamble is organized as follows:

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I. Executive Summary

A. Purpose and Summary of the Regulatory Action

The EPA is finalizing amendments to its 2012 and 2016 Rules affecting the oil and natural gas industry, titled, respectively, ''Oil and Natural Gas Sector: New Source Performance Standards and National Emission Standards for Hazardous Air Pollutants Reviews; Final Rule'' (''2012 Rule'') [1] and ''Oil and Natural Gas Sector: Emission Standards for New, Reconstructed, and Modified Sources; Final Rule'' (''2016 Rule'').[2] Those rules established NSPS for VOC emissions from the oil and natural gas industry, and the 2016 Rule also established NSPS for greenhouse gases (GHG), in the form of limitations on methane, for that industry.[3] The amendments that the EPA is finalizing are intended to continue existing protections from emission sources within the source category that the EPA originally listed for regulation under CAA section 111—termed the Oil and Natural Gas Production Source Category—while removing regulatory duplication.

In response to President Donald J. Trump's March 2017 Executive Order on Promoting Energy Independence and Economic Growth, the EPA has reviewed the 2012 and 2016 Rules with attention to whether they ''unduly burden the development of domestic energy resources beyond the degree necessary to protect the public interest or otherwise comply with the law'' and, thus, should be ''suspend[ed], revise[d], or rescind[ed]''.[4] [5] From this review, the EPA has determined that some of the requirements under those rules are inappropriate. For example, some of these requirements affect sources that are not appropriately identified as part of the regulated source category. In addition, some of the requirements under the 2016 Rule are unnecessary insofar as they impose redundant requirements. Accordingly, the EPA is acting to rescind those requirements while maintaining health and environmental protections from appropriately identified emission sources within the regulated source category.[6]

Specifically, the EPA is finalizing what it referred to as the primary proposal in the September 24, 2019, proposed action (''2019 Proposal''). Thus, this final rule contains two main actions. First, the EPA is finalizing a determination that the source category includes only the production and processing segments of the industry and is rescinding the standards applicable to the transmission and storage segment of the industry. This determination is based on the EPA's review of the original source category listing and its 2012 and 2016 Rules' interpretations of, and its 2016 Rule's revision to, the scope of the source category, which, as revised, covered sources in the transmission and storage segment. Having reexamined its prior rulemakings regarding the scope of this source category and the transmission and storage segment, the EPA has determined that the revision in the 2016 Rule of the original source category was not appropriate. Because the EPA is determining that the original source category did not cover the transmission and storage segment, and that this segment constitutes a separate source category from the production and processing segments, the EPA was authorized to list it for regulation under CAA section 111(b) only by making a cause-or-contribute-significantly and endangerment finding as required by the statute, which the EPA never did. Accordingly, in this first action, the EPA is rescinding the standards applicable to sources in the transmission and storage segment of the oil and natural gas industry.

Second, the EPA is separately rescinding the methane requirements of the NSPS applicable to sources in the production and processing segments. The EPA is concluding that those methane requirements are redundant with the existing NSPS for VOC and, thus, establish no additional health protections. The emission source control technologies that apply to the sources achieve reductions in both methane and VOC emissions, and the recordkeeping and other requirements overlap as well. Rescinding the applicability of the 2016 Rule requirements to methane emissions, while leaving the applicability to VOC emissions in place, will not affect the amount of methane emission reductions that those requirements will achieve.

This final rule also concludes that, as a prerequisite for newly regulating any air pollutant that the EPA did not consider when listing or initially regulating the source category, CAA section 111 requires the EPA to make a finding that emissions of that air pollutant from the source category cause or contribute significantly (which we term the significant contribution finding, or SCF) to air pollution which may reasonably be anticipated to endanger public health or welfare (which we sometimes refer to as dangerous air pollution). Further, the final rule determines that the SCF for methane that the EPA made in the alternative in the 2016 Rule was invalid and did not meet this statutory standard, for two reasons: (i) The EPA made that finding on the basis of methane emissions from the production, processing, and transmission and storage segments, instead of just the production and processing segments; and (ii) the EPA failed to support that finding with either established criteria or some type of reasonably explained and intelligible standard or threshold for determining when an air pollutant contributes significantly to dangerous air pollution. The fact that the 2016 Rule's SCF for methane was invalid provides another basis for rescinding the methane requirements for the

[1] 77 FR 49490 (August 16, 2012).

[2] 81 FR 35824 (June 3, 2016).

[3] Docket ID No. EPA–HQ–OAR–2010–0505.

[4] Executive Order 13783, ''Promoting Energy Independence and Economic Growth,'' section 1(c) (March 28, 2017); *see also* section 7(a) (specifically directing the EPA to review the 2016 Rule, ''and any rules and guidance issued pursuant to it, for consistency with the policy set forth in section 1 of this order and, if appropriate, [to], as soon as practicable, suspend, revise, or rescind the guidance, or publish for notice and comment proposed rules suspending, revising, or rescinding those rules'').

[5] 82 FR 16331 (April 4, 2017) (review of 2016 Rule pursuant to Executive Order 13783, signed by the EPA Administrator).

[6] We note that the EPA is addressing certain specific reconsideration issues—fugitive emissions requirements at well sites and compressor stations, well site pneumatic pump standards, and the requirements for certification of closed vent systems by a professional engineer (PE)—in a separate final rule. *See* Docket ID Item No. EPA–HQ–OAR–2010–0505–7730 and 82 FR 25730.

production and processing segments. While the EPA took comment in the 2019 Proposal on what criteria should inform its judgment as to whether a pollutant causes or contributes significantly to dangerous air pollution, the EPA is not taking further action on such criteria in this rulemaking.

B. Costs and Benefits

The EPA has projected the compliance cost reductions, emissions changes, and forgone benefits that may result from the final rule for the years of analysis, 2021 to 2030. The projected cost reductions and forgone benefits are presented in detail in the Regulatory Impact Analysis (RIA) accompanying this final rule. The EPA notes that the projected cost reductions and forgone benefits are directly associated with the rescission of the NSPS applicable to sources in the transmission and storage segment of the source category and not the rescission of methane from the production and processing segments.

A summary of the key results of this final rule is presented in Table 1.[7] Table 1 presents the present value (PV) and equivalent annualized value (EAV), estimated using discount rates of 7 and 3 percent, of the changes in benefits, costs, and net benefits, as well as the change in emissions under the final rule. Here, the EPA refers to the cost reductions as the ''benefits'' of this rule and the forgone benefits as the ''costs'' of this rule in Table 1. The net benefits are the benefits (cost reductions) minus the costs (forgone benefits).

TABLE 1—COST REDUCTIONS, FORGONE BENEFITS, AND FORGONE EMISSIONS REDUCTIONS OF THE FINAL RULE, 2021 THROUGH 2030

[Millions 2016$]

	7-Percent discount rate		3-Percent discount rate	
	PV	EAV	PV	EAV
Benefits (Total Cost Reductions)	$31	$4.1	$38	$4.3
Costs (Forgone Benefits)	17	2.2	63	7.2
Net Benefits [1]	14	1.9	−25	−2.9
Emissions	Forgone Reductions			
Methane (short tons)	400,000			
VOC (short tons)	11,000			
Hazardous Air Pollutant(s) (HAP) (short tons)	330			
Methane (million metric tons carbon dioxide equivalent (CO_2 Eq.))	9			

[1] **Note:** Estimates may not sum due to independent rounding.

This final rule is expected to result in benefits (compliance cost reductions) for affected owners and operators. The PV of these benefits (cost reductions), discounted at a 7-percent rate, is estimated to be about $31 million, with an EAV of about $4.1 million (Table 1). Under a 3-percent discount rate, the PV of cost reductions is $38 million, with an EAV of $4.3 million (Table 1).

The estimated costs (forgone benefits) include the monetized climate effects of the projected increase in methane emissions under the final rule. The PV of these climate-related costs (forgone benefits), discounted at a 7-percent rate, is estimated to be about $17 million, with an EAV of about $2.2 million (Table 1). Under a 3-percent discount rate, the PV of the climate-related costs (forgone benefits) is about $63 million, with an EAV of about $7.2 million (Table 1). The EPA also expects that there will be increases in VOC and HAP emissions as a result of this final rule. While the EPA expects that the forgone VOC emission reductions may also degrade air quality and adversely affect health and welfare effects associated with exposure to ozone, particulate matter with a diameter of 2.5 micrometers or less ($PM_{2.5}$), and HAP, we are unable to quantify these effects at this time. This omission should not imply that these forgone benefits do not exist. To the extent that the EPA were to quantify these ozone and particulate matter (PM) impacts, the Agency would estimate the number and value of avoided premature deaths and illnesses using an approach detailed in the Particulate Matter National Ambient Air Quality Standards (NAAQS) and Ozone NAAQS RIA (U.S. EPA, 2012; U.S. EPA, 2015).

The PV of the net benefits of this rule, discounted at a 7-percent rate, is estimated to be about $14 million, with an EAV of about $1.9 million (Table 1). Under a 3-percent discount rate, the PV of net benefits is about $−25 million, with an EAV of about $−2.9 million (Table 1).

II. General Information

A. Does this action apply to me?

Categories and entities potentially affected by this action include:

TABLE 2—INDUSTRIAL SOURCE CATEGORIES AFFECTED BY THIS ACTION

Category	NAICS code [1]	Examples of regulated entities
Industry	211120	Crude Petroleum Extraction.
	211130	Natural Gas Extraction.
	221210	Natural Gas Distribution.
	486110	Pipeline Distribution of Crude Oil.
	486210	Pipeline Transportation of Natural Gas.
Federal Government		Not affected.

[7] In a separate action, the EPA is finalizing technical reconsideration amendments to 40 CFR part 60, subpart OOOOa (EPA–HQ–OAR–2017–0483; FRL–10013–60–OAR; FR Doc. 2020–18115). These technical amendments where proposed in October 2018. 83 FR 52056. Please reference that final rule for the summary and rationale of those technical changes. Please refer to the RIA for both rules to see the combined impacts.

TABLE 2—INDUSTRIAL SOURCE CATEGORIES AFFECTED BY THIS ACTION—Continued

Category	NAICS code [1]	Examples of regulated entities
State/local/tribal government		Not affected.

[1] North American Industry Classification System (NAICS).

This table is not intended to be exhaustive, but rather provides a guide for readers regarding entities likely to be affected by this action. Other types of entities not listed in the table could also be affected by this action. To determine whether your entity is affected by this action, you should carefully examine the applicability criteria found in the final rule. If you have questions regarding the applicability of this action to a particular entity, consult the person listed in the **FOR FURTHER INFORMATION CONTACT** section, your air permitting authority, or your EPA Regional representative listed in 40 CFR 60.4 (General Provisions).

B. How do I obtain a copy of this document, background information, and other related information?

In addition to being available in the docket, an electronic copy of the final action is available on the internet. Following signature by the Administrator, the EPA will post a copy of this final action at *https://www.epa.gov/controlling-air-pollution-oil-and-natural-gas-industry.* Following publication in the **Federal Register**, the EPA will post the **Federal Register** version of the final rule and key technical documents at this same website. A redline version of the regulatory language that incorporates the final changes in this action is available in the docket for this action (Docket ID No. EPA–HQ–OAR–2017–0757). Additional background information about this final rule, including industry and emissions information, regulatory history, litigation background, other notable events, related Federal actions, and a comprehensive summary and rationale of the proposed options can be found at 84 FR 50244 (September 24, 2019).

C. Judicial Review

Under section 307(b)(1) of the CAA, judicial review of this final rule is available only by filing a petition for review in the United States Court of Appeals for the District of Columbia Circuit (''the Court'') by November 13, 2020. Moreover, under section 307(b)(2) of the CAA, the requirements established by this final rule may not be challenged separately in any civil or criminal proceedings brought by the EPA to enforce these requirements. Section 307(d)(7)(B) of the CAA further provides that ''[o]nly an objection to a rule or procedure which was raised with reasonable specificity during the period for public comment (including any public hearing) may be raised during judicial review.'' This section also provides a mechanism for the EPA to convene a proceeding for reconsideration, ''[i]f the person raising an objection can demonstrate to the EPA that it was impracticable to raise such objection within [the period for public comment] or if the grounds for such objection arose after the period for public comment (but within the time specified for judicial review) and if such objection is of central relevance to the outcome of the rule.'' Any person seeking to make such a demonstration to us should submit a Petition for Reconsideration to the Office of the Administrator, U.S. Environmental Protection Agency, Room 3000, WJC South Building, 1200 Pennsylvania Ave. NW, Washington, DC 20460, with a copy to both the person(s) listed in the preceding **FOR FURTHER INFORMATION CONTACT** section, and the Associate General Counsel for the Air and Radiation Law Office, Office of General Counsel (Mail Code 2344A), U.S. Environmental Protection Agency, 1200 Pennsylvania Ave. NW, Washington, DC 20460.

III. Background

The EPA reviewed the relevant background in the 2019 Proposal, including discussing the oil and natural gas industry and its emissions, 84 FR 50247 through 50; the statutory background, *Id.* at 50251; the regulatory history and litigation background regarding performance standards for the oil and natural gas industry, *Id.* at 50251 and 52; other notable events, including the March 28, 2017, Executive Order that led the EPA to initiate this rulemaking, *Id.* at 50252 and 53; and related state and Federal regulatory actions, *Id.* at 50253 and 54. The EPA incorporates that information by reference and will not repeat it here.

Since the 2019 Proposal, the EPA has updated information on the oil and natural gas industry emissions inventories based on the recently released Inventory of United States Greenhouse Gas Emissions and Sinks: 1990–2018 (published April 13, 2020) and the 2017 National Emissions Inventory (NEI) (released February 2020). In Tables 3 to 7 below, the EPA provides the updated estimate of emissions of methane, VOC, and sulfur dioxide (SO_2) from oil and natural gas industry sources.

Methane emissions in the U.S. and from the oil and natural gas industry. Official U.S. estimates of national level GHG emissions and sinks are developed by the EPA for the U.S. GHG Inventory (GHGI) to comply with commitments under the United Nations Framework Convention on Climate Change. The U.S. GHGI, which includes recent trends, is organized by industrial sectors. The oil and natural gas production, natural gas processing, and natural gas transmission and storage sectors emit 25 percent of U.S. anthropogenic methane. Table 3 below presents total U.S. anthropogenic methane emissions for the years 1990, 2008, and 2018.

TABLE 3—U.S. METHANE EMISSIONS BY SECTOR

[Million metric ton carbon dioxide equivalent (MMT CO_2 eq.)]

Sector	1990	2008	2018
Oil and Natural Gas Production, and Natural Gas Processing and Transmission and Storage	185	185	163
Oil and Natural Gas Production, and Natural Gas Processing	128	153	129
Oil and Natural Gas Transmission and Storage	57	32	34
Landfills	180	125	111

TABLE 3—U.S. METHANE EMISSIONS BY SECTOR—Continued

[Million metric ton carbon dioxide equivalent (MMT CO_2 eq.)]

Sector	1990	2008	2018
Enteric Fermentation	164	174	178
Coal Mining	97	76	53
Manure Management	37	54	62
Other Oil and Gas Sources	44	18	13
Wastewater Treatment	15	15	14
Other Methane Sources [8]	57	51	57
Total Methane Emissions	779	698	650

Emissions from the Inventory of United States Greenhouse Gas Emissions and Sinks: 1990–2018 (published April 13, 2020), calculated using global warming potential (GWP) of 25. *Note:* Totals may not sum due to rounding.

Table 4 below presents total methane emissions from natural gas production through transmission and storage and petroleum production, for years 1990, 2008, and 2018, in MMT CO_2 Eq. (or million metric tonnes CO_2 Eq.) of methane.

TABLE 4—U.S. METHANE EMISSIONS FROM NATURAL GAS AND PETROLEUM SYSTEMS

[MMT CO_2 eq.]

Sector	1990	2008	2018
Oil and Natural Gas Production and Natural Gas Processing and Transmission (Total)	185	185	163
Natural Gas Production	61	100	82
Natural Gas Processing	21	11	12
Natural Gas Transmission and Storage	57	32	34
Petroleum Production	45	42	35

Emissions from the Inventory of United States Greenhouse Gas Emissions and Sinks: 1990–2018 (published April 13, 2020), calculated using GWP of 25. *Note:* Totals may not sum due to rounding.

VOC and SO_2 emissions in the U.S. and from the oil and natural gas industry. Official U.S. estimates of national level VOC and SO_2 emissions are developed by the EPA for the NEI, for which states are required to submit information under 40 CFR part 51, subpart A. Data in the NEI may be organized by various data points, including sector, NAICS code, and Source Classification Code. The oil and natural gas sources emit 5.8 and 2.4 percent of U.S. VOC and SO_2, respectively. Tables 5 and 6 below present total U.S. VOC and SO_2 emissions by sector, respectively, for the year 2017, in kilotons (kt) (or thousand metric tons).

TABLE 5—U.S. VOC EMISSIONS BY SECTOR

[kt]

Sector	2017
Biogenics—Vegetation and Soil	25,823
Fires—Wildfires	4,578
Oil and Natural Gas Production, and Natural Gas Processing and Transmission	2,504
Fires—Prescribed Fires	2,042
Solvent—Consumer and Commercial Solvent Use	1,610
Mobile—On-Road non-Diesel Light Duty Vehicles	1,507
Mobile—Non-Road Equipment—Gasoline	1,009
Other VOC Sources [9]	4,045
Total VOC Emissions	43,118

Emissions from the 2017 NEI (released April 2020). *Note:* Totals may not sum due to rounding.

TABLE 6—U.S. SO_2 EMISSIONS BY SECTOR

[kt]

Sector	2017
Fuel Combustion—Electric Generation—Coal	1,319
Fuel Combustion—Industrial Boilers, Internal Combustion Engines—Coal	212
Mobile—Commercial Marine Vessels	183

[8] Other sources include rice cultivation, forest land, stationary combustion, abandoned oil and natural gas wells, abandoned coal mines, mobile combustion, composting, and several sources emitting less than 1 MMT CO_2 Eq. in 2018.

TABLE 6—U.S. SO_2 EMISSIONS BY SECTOR—Continued

[kt]

Sector	2017
Industrial Processes—Not Elsewhere Classified	138
Fires—Wildfires	135
Industrial Processes—Chemical Manufacturing	123
Oil and Natural Gas Production and Natural Gas Processing and Transmission	65
Other SO_2 Sources [10]	551
Total SO_2 Emissions	2,726

Emissions from the 2017 NEI (released April 2020). *Note:* Totals may not sum due to rounding.

Table 7 below presents total VOC and SO_2 emissions from oil and natural gas production through transmission and storage, for the year 2017, in kt (or thousand metric tons).

TABLE 7—U.S. VOC AND SO_2 EMISSIONS FROM NATURAL GAS AND PETROLEUM SYSTEMS

[kt]

Sector	VOC	SO_2
Oil and Natural Gas Production and Natural Gas Processing and Transmission (Total)	2,504	65
Oil and Natural Gas Production	2,478	41
Natural Gas Processing	12	23
Natural Gas Transmission and Storage	14	1

Emissions from the 2017 NEI, (published April 2020), in kt (or thousand metric tons). *Note:* Totals may not sum due to rounding.

IV. 2019 Proposal

On September 24, 2019, the EPA issued a proposed rulemaking (2019 Proposal) to amend the 2012 Rule and 2016 Rule for the oil and natural gas industry that would remove regulatory duplication and save the industry millions of dollars in compliance costs each year, while maintaining health and environmental protections from oil and natural gas sources that the Agency considers appropriate to regulate in this rule.[11] The EPA issued the proposal in response to President Trump's Executive Order on Promoting Energy Independence and Economic Growth. Generally speaking, that order directs agencies to review existing regulations that potentially ''burden the development or use of domestically produced energy resources,'' including oil and natural gas, and to suspend, revise, or rescind such regulatory requirements if appropriate. The proposal included a primary regulatory option and an alternative regulatory option. The primary option proposed to remove all sources in the transmission and storage segment of the oil and natural gas industry from regulation under the NSPS, both for VOC and for GHG. The primary option separately proposed to rescind the methane requirements in the 2016 Rule that apply to sources in the production and processing segments of the industry. The alternative option proposed to rescind the methane requirements that apply to all sources in the oil and natural gas industry, without removing any sources from the source category as defined in the 2016 Rule. The EPA additionally solicited comment on alternative interpretations of the EPA's legal authority to regulate pollutants under CAA section 111.

CAA section 111 requires the EPA to set NSPS for categories of stationary sources that the EPA has listed (''source categories'') because they cause, or significantly contribute to, air pollution that may reasonably be anticipated to endanger public health or welfare. The Agency's original source category listing for the oil and natural gas industry, issued in 1979, included only the crude oil and natural gas production and natural gas processing segments of the industry. However, in the 2012 Rule and 2016 Rule, the EPA interpreted the 1979 listing to have established the scope of the source category as including the industry's transmission and storage segment. In the 2016 Rule, the EPA also, as an alternative, expanded the source category to include the transmission and storage segment. In the 2019 Proposal, the EPA proposed to remove sources in the transmission and storage segment from the Oil and Natural Gas Production source category on the grounds that the Agency had erred in the 2012 and 2016 Rules when it had interpreted or expanded the source category, because the transmission and storage segment of the industry is functionally separate from the production and processing segment. The EPA further stated that a separate SCF would be necessary for that segment to be listed as a source category for regulation. The proposal further stated that the emissions limits that apply to sources in the transmission and storage segment in the 2012 Rule and 2016 Rule would be rescinded because that segment would be removed from the source category. Finally, the EPA proposed to rescind emissions requirements for methane for sources located in the production and processing segments on grounds that those requirements are redundant to the requirements for VOC. The proposal made clear that the emissions limits for VOC would remain for the production and processing segments.

In the alternative proposal, the EPA proposed to rescind the methane requirements in the 2016 Rule for all oil and natural gas sources, without removing the transmission and storage sources from the source category. Under this alternative, the rule would retain VOC standards for the production, processing, and transmission and storage segments of the industry. As with the primary proposal, the alternative proposal is based on the view that because the controls to reduce VOC emissions also reduce methane, separate methane requirements for the industry are redundant.

The EPA further stated that the proposed amendments would remove the Agency's obligation to develop emission guidelines (EG) to address methane emissions from existing sources under section 111(d) of the CAA. The EPA stated its belief that not

[9] Other sources include remaining sources emitting less than 1,000 kt VOC in 2017.

[10] Other sources include remaining sources emitting less than 100 kt SO_2 in 2017.

[11] 84 FR 50244.

regulating existing sources would have limited environmental impact, because some existing sources will ''modify'' such that they will become subject to requirements for new sources, and because the number of remaining sources may decline over time as they are shut down or become obsolete.

The EPA also took comment on an alternative interpretation of its legal authority to regulate pollutants under CAA section 111. In the 2016 Rule, the EPA took the position that the law did not require the Agency, as a prerequisite to regulating methane as part of the NSPS, to first make a separate determination that GHG emissions from the oil and natural gas industry cause, or significantly contribute to, dangerous air pollution (a pollutant-specific SCF). However, the Agency also made a finding in the alternative that if the CAA were interpreted to require a pollutant-specific SCF, then GHG emissions from the Oil and Natural Gas source category do cause or contribute significantly to dangerous air pollution. The 2019 Proposal solicited comment on three issues: (1) Whether the Agency should revise the interpretation it took in the 2016 Rule, so that CAA section 111 requires the EPA to make a pollutant-specific SCF for GHG emissions from the oil and natural gas industry as a predicate to regulation; (2) whether, if CAA section 111 does require a pollutant-specific SCF, whether the finding in the alternative in the 2016 Rule satisfied that requirement; and (3) what, if any, specific criteria the EPA should use to make a pollutant-specific SCF.

The EPA solicited comments on all aspects of the proposal during a 60-day public comment period. The EPA held a public hearing in Dallas, Texas, in October 2019; 105 speakers provided oral testimony and 32 observers attended. The EPA received almost 300,000 public comments on the proposed rule. The EPA is not responding to any late comment received.

V. Final Action and Rationale

A. Summary of Final Action

The EPA is finalizing what was referred to as the primary proposal in the 2019 Proposal. First, the final rule removes all sources in the transmission and storage segment of the oil and natural gas industry from regulation under the NSPS and removes all emissions limitations for both VOC and GHG for sources in the transmission and storage segment. Second, the final rule separately rescinds the standards for methane emissions in the 2016 Rule that apply to sources in the production and processing segments of the industry. Third, the final rule articulates the EPA's interpretation that under CAA section 111(b)(1)(A), as a prerequisite for newly regulating any air pollutant, the Agency is required to make a finding that emissions of the air pollutant, from the source category, cause or contribute significantly to air pollution which may reasonably be anticipated to endanger public health or welfare. Further, the final rule concludes that the alternative SCF made by the EPA in the 2016 Rule was invalid and did not meet this statutory standard.

B. Rationale

1. Revision of the Source Category To Remove Transmission and Storage Segment

As noted above, the EPA is finalizing its proposal to remove the transmission and storage segment entirely from the source category and rescind the NSPS requirements applicable to sources within that segment. This final action is based on the EPA's determination that its 2012 and 2016 rulemakings that interpreted or expanded the source category to include sources in that segment were improper. The following discussion provides background on CAA section 111, the history of the Oil and Natural Gas Production source category, and the rationale for this final decision.

Under CAA section 111(b)(1)(A), the EPA must ''publish . . . a list of categories of stationary sources, emissions from which, in the judgment of the Administrator, cause[ ], or contribute[ ] significantly to, air pollution which may reasonably be anticipated to endanger public health or welfare.'' Further, CAA section 111(b)(1)(A) directs that ''from time to time thereafter'' the EPA ''shall revise'' this ''list'' of categories of stationary sources. Following the ''inclusion of a category of stationary sources in a list,'' the EPA then proposes and promulgates ''standards of performance for new sources within such category.'' CAA Section 111(b)(1)(B). Thereafter, the EPA ''shall . . . review and, if appropriate, revise such standards.'' *Id.*

CAA section 111(b)(1)(A) does not include any specific criteria for determining the reasonable scope of a given ''category'' of ''stationary sources'' beyond the requirement that the Administrator make a finding that, in his or her ''judgment,'' emissions from the ''category of sources . . . cause[ ], or contribute[ ]significantly to, air pollution which may reasonably be anticipated to endanger public health or welfare.'' Accordingly, the EPA is afforded some measure of discretion in determining at the outset the scope of a source category.

In 1978, the EPA published ''Priorities for New Source Performance Standards Under the Clean Air Act Amendments of 1977.''[12] The purpose of this document was to implement the requirements of CAA section 111(f) to develop and apply a methodology for identifying, establishing, and prioritizing the source categories that should be considered first for in-depth analysis prior to NSPS promulgation under CAA section 111. For purposes of the 1978 analysis, the EPA aggregated emissions from ''oil and gas production fields'' and ''natural gas processing'' as part of the ''Crude Oil and Natural Gas Production Plant'' source category. The EPA identified this aggregated source category as a major source of hydrocarbon (HC) and SO_2 emissions. When the EPA finalized the priority list in 1979, it revised the name of the source category as ''Crude Oil and Natural Gas Production.'' 49 FR 49222 (August 21, 1979).

In 1985, the EPA promulgated two rulemakings establishing NSPS for the Crude Oil and Natural Gas Production source category. These were 40 CFR part 60, subpart KKK—Standards of Performance for Equipment Leaks of VOC from Onshore Natural Gas Processing Plants (50 FR 26124, June 23, 1985); and subpart LLL—Standards of Performance for SO_2 Emissions from Onshore Natural Gas Processing (50 FR 40160, October 1, 1985). When it first proposed 40 CFR part 60, subpart KKK, the EPA noted that the ''crude oil and natural gas production industry encompasses the operations of exploring for crude oil and natural gas products, removing them from beneath the earth's surface, and processing these products for distribution to petroleum refineries and gas pipelines.''[13] The EPA repeated that description of the identified source category when it proposed 40 CFR part 60, subpart LLL, explaining that the ''crude oil and natural gas production industry encompasses not only processing of the natural gas (associated or not associated with crude oil) but operations of exploration, drilling, and subsequent removal of the gas from porous geologic formations beneath the earth's surface.''[14]

In 2012, the EPA reviewed the VOC and SO_2 standards and at the same time

[12] Priorities for New Source Performance Standards Under the Clean Air Act Amendments of 1977. April 1978. EPA–450/3–78–019.

[13] 49 FR 2637 (January 20, 1984).

[14] 49 FR 2658 (January 20, 1984).

established new requirements for additional stationary sources of VOC emissions that had not been regulated in the 1985 rulemaking (*e.g.,* well completions, pneumatic controllers, storage vessels, and compressors)—''Oil and Natural Gas Sector: New Source Performance Standards and National Emission Standards for Hazardous Air Pollutants Reviews—Final Rule'' (77 FR 49490, August 16, 2012). In the preamble of the 2011 proposal for the 2012 Rule, the EPA interpreted the 1979 listing as indicating that ''the currently listed Oil and Natural Gas source category covers all operations in this industry (*i.e.,* production, processing, transmission, storage and distribution).'' ''Oil and Natural Gas Sector: New Source Performance Standards and National Emission Standards for Hazardous Air Pollutants Reviews—Proposed Rule,'' 76 FR 52738, 52745 (August 23, 2011). Further, the EPA stated that ''[t]o the extent there are oil and gas operations not covered by the currently listed Oil and Natural Gas source category. . . ., we hereby modify the category list to include all operations in the oil and natural gas sector.'' *Id.* The stated basis for that proposed decision was that ''[s]ection 111(b) of the CAA gives the EPA the broad authority and discretion to list and establish NSPS for a category that, in the Administrator's judgment, causes or contributes significantly to air pollution which may reasonably be anticipated to endanger public health or welfare.'' *Id.* No additional discussion of this listing position was provided in the 2011 proposal.

In the 2012 final rulemaking, the EPA promulgated NSPS for emission sources in the production, processing, and transmission and storage segments, 77 FR 49492, and stated that ''[t]he listed Crude Oil and Natural Gas Production source category covers, at a minimum, those operations for which we are establishing standards in this final rule.'' *Id.* at 49496. In responding to comments, the EPA took the position that it was not actually revising the source category to include emission sources in the transmission and storage segment, but rather, was interpreting the 1979 listing to be ''broad,'' and interpreting the 1985 rulemaking as ''view[ing] this source category listing very broadly,'' *Id.* at 49514, so that, in the EPA's view, the source category was already sufficiently broad to include that segment.[15]

In 2016, the EPA promulgated additional NSPS (40 CFR part 60, subpart OOOOa) for the Crude Oil and Natural Gas Production source category (81 FR 35824, June 3, 2016). As the EPA did in the 2012 Rule, the EPA took the position that the 1979 listing was broad enough to encompass the transmission and storage segment and that the 1985 rulemakings confirmed that broad listing. 81 FR 35832 (''The scope of the 1978 Priority List is further demonstrated by the Agency's pronouncements during the NSPS rulemaking that followed the listing.''). The EPA stated that the inclusion of the transmission and storage segment into the original 1979 source category was warranted because equipment and operations at production, processing, transmission and storage facilities are a sequence of functions that are interrelated and necessary for getting the recovered gas ready for distribution. Nevertheless, the EPA recognized that the scope of the prior listing may have had some ambiguity. Accordingly, ''as an alternative,'' the EPA finalized a revision of the category to broaden it, so that ''[a]s revised, the listed oil and natural gas source category includes oil and natural gas production, processing, transmission, and storage'' and the EPA changed the source category name to be ''Crude Oil and Natural Gas source category.'' (81 FR 35840).

a. Scope of 1979 Listing Action

For this final rule, the EPA has reviewed the original 1979 listing of the Crude Oil and Natural Gas Production source category and the associated background materials and now finds that its 2012 and 2016 interpretation of the 1979 listing (*i.e.,* that the 1979 listing included natural gas transmission and storage) was erroneous. *See F.C.C.* v. *Fox Television Stations, Inc.,* 556 U.S. 502 (2009) (an agency may revise its policy, but must demonstrate that the new policy is permissible under the statute and is supported by good reasons, taking into account the record of the previous rule). The EPA received comments on the 2019 Proposal concerning this issue and the associated rationale. These comments are provided, along with the EPA's responses, in section VIII.A of this preamble and in Chapter 5 of the Response to Comments Document for this action. None of the comments received resulted in a change in the EPA's rationale and conclusions from proposal. The following explains our decision.[16]

While the EPA has listed source categories that are broad,[17] the silence of the 1979 listing as to the transmission and storage segment suggests that the segment was *not* considered for inclusion at the time of the listing. Principles of administrative law require that in order for something (in this case, the transmission and storage segment) to be subject to regulation, the EPA should provide for and explain such regulation clearly. Moreover, where the EPA has remained silent on any explanation for its choice of regulation, the Court has held, ''a rule without a stated reason is necessarily arbitrary and capricious.'' *Small Refiner Lead Phase-Down Task Force* v. *U.S. EPA,* 705 F.2d 506, 551 (1983). Accordingly, if the EPA had intended for the 1979 listing to include the transmission and storage segment, the Agency's failure to explain that decision would have rendered it arbitrary and capricious. It is reasonable to presume that the Agency did not act arbitrarily and capriciously, and, therefore, that its silence regarding the transmission and storage segment indicated that it did not intend to cover that segment in the 1979 listing.

Additionally, to the extent there was ambiguity in the original 1979 listing, the EPA made clear its interpretation in 1984, when the EPA proposed to set the first standards of performance for sources within the Crude Oil and Natural Gas Production source category (*i.e.,* 40 CFR part 60, subpart KKK). The views the Agency expressed concerning the scope of the source category are particularly relevant because this rulemaking was conducted shortly after the listing and because it established the initial NSPS. In this proposal, the EPA described the category as ''encompass[ing] the operations of exploring for crude oil and natural gas products, removing them from beneath the earth's surface and processing these products for distribution to petroleum refineries and gas pipelines,'' but this description made no reference to the subsequent activities of transmission

[15] In the 2012 Rule rulemaking, the EPA referred to the distribution segment of the oil and natural gas industry, which entails transporting natural gas to the end user. 76 FR 52738, 52745 (August 23, 2011) (proposed rule); 77 FR 49514, 77 FR 49493 (Table 2) (August 16, 2012) (final rule). However, in the 2016 Rule, the EPA clarified that the scope of the Oil and Natural Gas Production and Processing source category includes the transmission and storage segment, but not the distribution segment. In addition, the EPA has never treated any sources in the distribution segment as subject to the requirements of NSPS subpart OOOO or OOOOa.

[16] In 1979, the EPA named the source category ''Crude Oil and Natural Gas Production source category.'' In 2016, the EPA changed the source category name to be ''Crude Oil and Natural Gas source category.'' Because this final rule rescinds the 2016 expansion, the EPA is finalizing the source category's name back to how it read in 1979.

[17] The EPA also has listed narrow source categories, as noted in section VIII.A of this preamble.

and storage of crude oil and natural gas products.[18] This description is reasonably read to establish that sources in the transmission and storage segment were not included in the Crude Oil and Natural Gas Production source category as listed in 1979.

Similarly, in the same sentence, the EPA defined the scope of the source category as encompassing oil operations up to the point of distribution to petroleum refineries, which are a separate source category. In this manner, the EPA indicated that the Crude Oil and Natural Gas Production source category includes operations from well sites (exploration, drilling, and removal) and natural gas processing plants (processing). While gathering and boosting compressor stations were not specified, it is reasonable to conclude that they are also included because they are located between two covered sites, the well site and the processing plant. However, to reiterate, subsequent operations, such as transmission and storage, and distribution were not included.

In the 1984 proposal, the EPA added that ''there are several VOC emission points within this industry,'' which the Agency categorized as process, storage, and equipment leaks. 49 FR 2637. In the 2016 NSPS, the EPA used this description of the three sets of emission points as support for the proposition that the Agency previously intended the source category to include transmission and storage. Specifically, the EPA stated that ''these emissions can be found throughout the various segments of the natural gas industry.'' 81 FR 35832. The EPA has closely reexamined the language of the 1984 proposal and found that, importantly, in the descriptions of these three categories of emission points, it is clear that the EPA considered these emission sources only in the production and processing segments. Therefore, while it is true that there are process, storage, and equipment leak emissions throughout the oil and natural gas sector, the discussion in the 1984 proposal entirely focused on these sources in the production and processing segments, and made no reference to the transmission and storage segment. The following discusses each of those three sets of sources in more detail.

With respect to process sources, the 1984 proposal states that they include well systems, field oil and natural gas separators, wash tanks, settling tanks, and other sources. The proposal further states that process sources remove the crude oil and natural gas from beneath the earth and separate gas and water from the crude oil. 49 FR 2637. This description of the process emission point clearly refers to the production and processing segments and is silent concerning the transmission and storage segment.

For the second set of emission points, storage sources, the 1984 proposal states that they include field storage tanks, condensate tanks, and cleaned oil tanks. These tanks emit VOC, the pollutant addressed in the 1984 proposal. These three types of tanks are common in the production segment and/or at natural gas processing plants; as gas is separated from oil, condensate and impurities, these tanks are used to store oil and condensate, which contain VOC. As such, these tanks are storage sources of VOC emissions. In contrast, storage at natural gas transmission and storage facilities refers to storage of gas, mostly in the underground storage reservoirs. Because the gas stored in underground reservoirs is pipeline quality natural gas (95–98 percent methane), these storage facilities in the transmission and storage segment are not emission points of concern for VOC, or any of the other pollutants identified in the 1984 proposal as being emitted from the oil and gas industry. Additionally, the cited discussion in the proposal made no explicit mention of transmission and storage facilities. Furthermore, there are no oil tanks or field tanks in the transmission and storage segment. As for condensate tanks, these tanks are rarely used at the transmission and storage segment because, as mentioned above, the gas that enters this segment is pipeline quality gas and, therefore, contains little to no condensate. Given the reference in the 1984 proposal to two other types of tanks that are also commonly found in the production and processing segments but absent in the transmission and storage segment, it is reasonable to conclude that the proposal's reference to condensate tanks was also intended to be limited to the production and processing segments. For all of these reasons, the better reading of the 1984 proposal discussion on storage tanks is that it was limited only to such tanks located in the production and processing segments, and was not intended to encompass tanks located in the transmission and storage segment.

Similarly, the 1984 proposal describes the equipment leak emission points as referring to the production and processing segments of the Oil and Natural Gas source category and is silent concerning the transmission and storage segment. The proposal explains that equipment leaks of VOC can occur from ''pumps, valves, compressors, open ended lines or valves, and pressure relief devices used in onshore crude oil and natural gas *production* (emphasis added).'' *Id.* Additionally, the preamble acknowledges that there is equipment used in crude oil and natural gas production and distinguishes this from equipment used in natural gas processing. The EPA examined the use of leak detection and repair work practices for equipment leaks of VOC at natural gas processing plants and explained in the preamble that the costs and emission reduction numbers for the application of these techniques at the ''widely dispersed'' crude oil and natural gas production sites were not known at that time. In this manner, the EPA clearly acknowledged the existence of equipment leaks at both the production and processing segments. In contrast, although equipment leaks do occur in the transmission and storage segment, the proposal makes no mention of leaks in that segment. Thus, each of the three sets of emission sources under consideration in the 1984 proposal clearly is in the production and processing segments, and the proposal is silent about the transmission and storage segment.

Another indicator that the 1984 proposal did not consider transmission and storage lies in the fact that this proposal addressed VOC emissions. As discussed below, the composition of the natural gas in the transmission and storage segment is significantly different than in the production and processing segments, as the transmission and storage segment contains considerably less VOC, and as a result, sources in that segment emit low amounts of VOC. In many areas of the country, particularly those that produce liquids and associated gas, the production and processing segments have high VOC-content gases, but the transmission and storage operations have substantially lower VOC-content gases. In light of the fact that the 1979 listing concerned VOC content (termed, at that time, HC), this difference between the segments further supports the view that the EPA would not have included transmission and storage in the 1979 listing. This corroborates that the proposal did not consider emission sources related to the transmission and storage of natural gas. Thus, although process, storage, and equipment leaks are emission sources that are present across the industry, including in natural gas transmission and storage, additional examination of the 1984 proposal makes it clear that it considered process, storage, and equipment leaks in only the production

[18] 49 FR 2637; *see* also 49 FR 2658.

and processing segments of the oil and natural gas industry.

For the reasons noted above, the EPA concludes that its statements in the 2012 and 2016 Rules that the 1979 listing of the Crude Oil and Natural Gas Production source category included the transmission and storage segment, and that the 1984 proposal confirmed that action, were in error. Rather, the record of the 1979 action indicates that the source category did not include that segment, and the Agency confirmed that narrower scope of the source category in its 1984 proposal to promulgate the initial set of NSPS.

b. Operations in the Transmission and Storage Segment Are Distinctly Different

As noted above, the 2016 Rule stated that the ''1979 listing of [the Crude Oil and Natural Gas Production] source category provides sufficient authority for this action'' to promulgate NSPS for sources in the transmission and storage segment, but then added that, ''to the extent that there is ambiguity in the prior listing, the EPA hereby . . ., as an alternative, . . . revis[es] . . . the category listing to broadly include the oil and natural gas industry.''[19] ''As revised,'' the 2016 Rule continued, ''the listed oil and natural gas category includes oil and natural gas production, processing, transmission, and storage.''[20] As discussed in the following paragraphs, the EPA is concluding, in line with the 2019 Proposal, that this alternative approach of revising the scope of the source category to include sources within the transmission and storage segment was also in error and should be rejected.

The EPA received comments on this issue, including the associated rationale. These comments are provided, along with the EPA's responses, in section VIII.A of this preamble and in Chapter 5 of the Response to Comments Document for this action. None of the comments received resulted in a change in the EPA's rationale and conclusions from proposal.

While CAA section 111(b)(1)(A) and (B) respectively authorize the EPA to ''revise,'' where warranted, both the ''list of source categories'' and ''standards of performance'' that the EPA has promulgated, nothing in CAA section 111 expressly authorizes or directs the EPA to ''revise'' a particular ''source category'' by altering its scope once the EPA has listed that source category. However, the EPA has inherent authority to reconsider, repeal, or revise past decisions, to the extent permitted by law, so long as the Agency provides a reasoned explanation. *See Sang Seup Shin* v. *INS,* 750 F.2d 122, 130 (D.C. Cir. 1984) (in absence of specific statutory prohibition, an agency has inherent authority to reconsider its decisions). The CAA complements the EPA's inherent authority to reconsider prior rulemakings by providing the Agency with broad authority to prescribe regulations as necessary, under CAA section 301(a). Even so, the authority to revise the scope of a source category must be exercised within reasonable boundaries and cannot be employed in a way that results in an unreasonable expansion of an existing source category. For the reasons discussed below, the EPA is not authorized to expand the scope of a listed source category to cover a new set of sources that are not sufficiently related to the sources in the pre-existing category, so that they constitute a separate source category for which the EPA would be required to make a new SCF and endangerment finding under CAA section 111(b)(1)(A) as a prerequisite to regulating them. Otherwise, expanding the source category by including new sources could be used to circumvent that requirement.

The EPA proposed to determine that the operations in the transmission and storage segment are not sufficiently related to the production and processing segments that were included in the original source category listing. In the 2016 Rule, the EPA held that the source category should be expanded because equipment and operations at production, processing, and transmission and storage facilities are a sequence of functions that are interrelated and necessary for getting the gas ready for distribution. In the 2019 Proposal, the EPA proposed to determine that this 2016 finding was unreasonable and proposed that transmission and storage operations are distinct from production and processing operations because (among other things) the natural gas that enters the transmission and storage segment has different composition and characteristics than the natural gas that enters the production and processing segments. 84 FR 50257.

While CAA section 111 does not define the term ''source category'' or use the phrase ''sufficiently related,'' this concept is inherent in the everyday definition of ''category.'' Merriam-Webster defines ''category'' as ''any of several fundamental and distinct classes to which entities or concepts belong,''[21] and it defines a ''class[ ]'' as ''a group, set, or kind sharing *common* attributes'' (emphasis added).[22] Commenters point out what they view as commonalities among both the production and processing and transmission and storage segments. These comments implicitly acknowledge that, to be a ''category,'' the associated sources must have something in common, that is, they must be sufficiently related to merit being associated as part of the same category. The EPA may not have articulated the ''sufficiently related'' test in those terms in prior actions, but, again, that test is implicit in the everyday meaning of ''category.'' That is, for items to be part of a ''category'' they must have key things in common, and if they have substantial differences, they should not be included in the same category. Without this test, it would be difficult to develop a basis for ascertaining the scope of a category. For this reason, the EPA has in effect regularly applied this test. For example, fugitive VOC emissions from leaking equipment occurs across several industries, including the synthetic organic chemical manufacturing industry and the petroleum refinery industry, but there are substantial enough differences between those industries to warrant putting them in separate source categories, notwithstanding the fact that some of their equipment is similar. For another example, when proposing to expand the original Asphalt Roofing Plants source category listing to include other locations where the preparation of asphalt for roofing may take place, such as oil refineries, the EPA stated that, ''the emissions, processes, and applicable controls for blowing stills and asphalt storage tanks at oil refineries and asphalt processing plants are the same as those at asphalt roofing plants. It is therefore reasonable to treat the asphalt processing and roofing manufacture industry as a single category of sources for the purposes of establishing standards of performance.'' 45 FR 76428. By finding commonality in emissions, processes, and applicable controls for these otherwise different sources, the EPA determined that they should be part of the same source category.

[19] 81 FR 35833.

[20] *Id.* (footnote omitted).

[21] ''Category.'' *Merriam-Webster.com Dictionary,* Merriam-Webster, *https://www.merriam-webster.com/dictionary/category.* Accessed 21 May, 2020.

[22] ''Class.'' *Merriam-Webster.com Dictionary,* Merriam-Webster, *https://www.merriam-webster.com/dictionary/class.* Accessed 19 May, 2020.

In contrast, based on a reexamination of the processes and operations found in the transmission and storage segment, the EPA is finalizing its determination that transmission and storage sources are, in fact, sufficiently distinct from production and processing sources so that the Agency erred when, in the 2016 Rule, it revised the source category to include sources in the transmission and storage segment. Specifically, the EPA now concludes that the processes and operations found in the transmission and storage segment are distinct from those found in the production and processing segments because the purposes of the operations are different and because the natural gas that enters the transmission and storage segment has different composition and characteristics than the natural gas that enters the production and processing segments.

The primary operations of the production and processing segments are exploring crude oil and natural gas products beneath the earth's surface, drilling wells to extract these products, and processing the crude oil and field gas for distribution to petroleum refineries and natural gas pipelines. As stated previously in this section, the EPA described this source category's operations similarly when proposing 40 CFR part 60, subpart KKK, in 1984. 49 FR 2637. The primary purpose of these segments is to obtain the product and then, in the case of natural gas, to remove impurities from the extracted product. At a well site (production segment), crude oil and natural gas are extracted from the ground. Some processing can take place at the well site, such as the physical separation of gas, production fluids, and condensate. Of these products, crude oil and natural gas undergo successive, separate processing. Crude oil is separated from water and other impurities and transported to a refinery via truck, railcar, or pipeline. The EPA treats oil refineries as a separate source category, accordingly, for present purposes, the oil component of the production segment ends at the point of custody transfer at the refinery.[23] The separated gas (''field gas'') is then sent through gathering pipelines to the natural gas processing plant (processing segment).[24] At the processing plant, the field gas is converted to sales gas or pipeline quality gas. This involves several steps, including the extraction of natural gas liquids (*e.g.,* a mixture of propane, butane, pentane) from the field gas, the fractionation of these natural gas liquids into individual products (*e.g.,* liquid propane), or both extraction and fractionation. The final natural gas that exits in the processing plant is sales gas, which is predominantly methane. In these segments, the field gas has physically changed such that it is a usable product.

The operations of the production and processing segments differ from the transmission and storage segment operations because in the latter, the natural gas does not undergo changes in composition, except for some limited removal of liquids that condensed during the temperature and pressure changes as the natural gas moves through the pipeline. Therefore, the natural gas that enters the transmission and storage segment has approximately the same composition and characteristics as the natural gas that leaves the segment for distribution. The segment includes natural gas transmission compressor stations, whose primary operation is to move the natural gas through transmission pipelines by increasing the pressure. Dehydration, which can also occur at compressor stations, is a secondary operation used when the natural gas has collected water during transmission. As discussed in the 2019 Proposal, this differs from the significant natural gas processing in the production and processing segments, which involves a series of processing steps dependent on factors such as the type of natural gas (*e.g.,* wet or dry gas), market conditions, and company contract specifications. 84 FR 50258. At storage facilities, natural gas is injected into underground storage for use during peak seasons.[25] When demand increases, the natural gas is extracted from the underground storage, dehydrated to remove water that has entered during storage, compressed, and moved through distribution pipelines.

Analysis of the composition of natural gas on a nationwide basis in the various industry segments confirms the different character of the segments. In 2011 and subsequently in 2018, the EPA conducted an analysis of the composition, expressed in percent volume, of natural gas based on the methane, VOC, and HAP content across the various industry segments.[26 27] For example, in 2011, the nationwide composition for the production segment, which included wells and unprocessed natural gas, consisted of approximately 83-percent methane, 4-percent VOC, and less than 1-percent HAP. In contrast, the transmission segment, which included pipeline and sales gas (*i.e.,* post processing), consisted of approximately 93-percent methane, 1-percent VOC, and less than 0.01-percent HAP. In 2018, the EPA reviewed new studies available and found similar results for the production segment. The nationwide composition for the production segment consisted of approximately 88-percent methane and 4-percent VOC. At proposal in 2019, we concluded that these differences in the gas composition demonstrated that the emissions profile is different following gas processing. After proposal in 2019, the EPA conducted a comprehensive analysis of data reported directly to the Greenhouse Gas Reporting Program (GHGRP) for reporting years 2015 through 2018 to determine whether the composition of natural gas, in terms of methane content, is statistically different between industry segments.[28] In order to determine whether the methane content is statistically different between industry segments, the analysis evaluated the average methane concentration for each segment based on the 2015–2018 GHGRP reporting data.[29]

[23] *See* 40 CFR part 60, subparts J and Ja, and 40 CFR part 63, subparts CC and UUU.

[24] Natural gas with high methane content is referred to as ''dry gas,'' while natural gas with significant amounts of ethane, propane, or butane is referred to as ''wet gas.'' The degree and location of processing is dependent on various factors, one being the type of natural gas (*e.g.,* wet or dry gas). In some ''dry gas'' areas, the field gas, with naturally higher methane content, may go from the well site directly into the transmission and storage segment without processing in a gas processing plant. The fact that some produced natural gas does not require processing and can be transported directly into the transmission and storage segment does not diminish the differences between the production and processing segments, on the one hand, and the transmission and storage segment, on the other. Rather, it just means that some gas does not need to go through the processing segment.

[25] Storage can also take place in above ground storage vessels; however, it is the EPA's understanding that these are more commonly used after the local distribution company custody transfer (LDC) or commonly ''city gate,'' which has not been included in the source category at any point. The term ''local distribution company custody transfer,'' defined in 40 CFR part 60, subpart OOOOa, means a metering station where the LDC receives a natural gas supply from an upstream supplier, which may be an interstate transmission pipeline or a local natural gas producer, for delivery to customers through the LDC's intrastate transmission or distribution lines. This final rule adds the definition of LDC to 40 CFR part 60, subpart OOOO.

[26] Memorandum to Bruce Moore, U.S. EPA from Heather Brown, EC/R. ''Composition of Natural Gas for use in the Oil and Natural Gas Sector Rulemaking.'' July 2011. Docket ID Item No. EPA–HQ–OAR–2010–0505–0084.

[27] Memorandum to U.S. EPA from Eastern Research Group. ''Natural Gas Composition.'' November 13, 2018. Docket ID No. EPA–HQ–OAR–2017–0757.

[28] Memorandum. Analysis of Average Methane Concentrations in the Oil and Gas Industry Using Data Reported Under 40 CFR part 98 Subpart W. April 9, 2020. Included in Docket ID No. EPA–HQ–OAR–2017–0757.

[29] See Table 17 of Memorandum. Analysis of Average Methane Concentrations in the Oil and Gas

For oil and natural gas production, the analysis estimated an average methane content of 69 and 83 percent, respectively. For gathering and boosting,[30] the analysis estimated an average methane content of 81 percent, and for gas processing, an average methane content of 78 percent. The analysis estimated an average methane content of 94 percent for transmission and 95 percent for storage. The analysis performed additional calculations and statistical assessments to generate the final statistical analysis and subsequent conclusions.

This analysis found that there is a substantial difference in methane concentrations between (1) gas production, gathering and boosting, and gas processing and (2) transmission and storage. This agrees with earlier data and analyses and the conclusion that there is a difference in the emissions profile between the production and processing segments and the transmission and storage segment.

It should be noted that in regulating HAP from the oil and natural gas industry, the EPA created separate source categories for the production and processing segments, regulated under subpart HH of 40 CFR part 63; and the transmission and storage segment, regulated under subpart HHH of 40 CFR part 63. *See* 64 FR 32610, June 17, 1999. In addition, the EPA has made a similar distinction between other source categories with segments that handle the production and processing of a material and subsequent transport of the product. As the EPA noted in the 2019 Proposal, 84 FR 50258, one example is the petroleum industry, in which production facilities,[31] refineries,[32] and bulk gasoline terminals [33] all have operational differences, and the EPA placed them in three different source categories. Those operational differences are similar to the operational differences between the production and processing segments and the transmission and storage segment at issue in this final rule.

It should be noted that in the 2016 Rule, the EPA justified including the transmission and storage segment in the Crude Oil and Natural Gas source category partly because some similar equipment (*e.g.,* storage vessels, pneumatic pumps, compressors) is used across the industry. While that is true, the differences in the operations of, and the differences in emission profiles of, the different segments support excluding the transmission and storage segment from the source category. A review of 2016 Rule compliance reports from sources in the EPA Regions (3, 6, 8, 9, and 10) with the greatest oil and natural gas activity indicates that there were no storage vessels emitting more than 6 tons per year (tpy) VOC reported in the transmission and storage segment.[34] Therefore, even though there are storage vessels in the transmission and storage segment, the liquids (condensate) stored and the throughputs are such that the VOC emissions are significantly different. This supports our understanding that VOC emissions are lower in the transmission and storage segment and that any gas processing that occurs in the transmission and storage segment generally is limited to removing liquids that condensed during the temperature and pressure changes as the gas moves through the pipeline. In addition, there are types of equipment present in the production segment (*e.g.,* oil tanks, three-phase separators) and processes at natural gas processing plants (*e.g.,* natural gas liquid extraction, natural gas liquids fractionation, sulfur and CO_2 removal) that are either not present or uncommon at natural gas transmission and storage facilities.

In summary, there are distinct differences in the operations between oil and natural gas production and natural gas processing, on the one hand, and natural gas transmission and storage, on the other. The primary operations of the production and processing segments are exploring crude oil and natural gas products beneath the earth's surface, drilling wells that are used to extract these products, and processing the crude oil and field gas for distribution to petroleum refineries and natural gas pipelines. The operations of the production and processing segments differ from the transmission and storage segment operations because in the latter, the natural gas does not undergo changes in composition, except for some limited removal of liquids that condensed during the temperature and pressure changes as the natural gas moves through the pipeline. Second, there are statistically significant differences in the emissions profiles between the production and processing segments and the transmission and storage segment. Third, there are equipment types and processes present in the oil and natural gas production and processing segments that are not present, or not common, at natural gas transmission and storage facilities. The EPA is, therefore, finalizing a revised source category which excludes transmission and storage sources from the Crude Oil and Natural Gas Production source category.

As the EPA stated in the 2019 Proposal, the 2016 Rule's expansion of the source category to include sources in the transmission and storage segment did, in fact, exceed the reasonable boundaries of the EPA's authority to revise source categories. 81 FR 35833. The 2016 Rule also erred in purporting to list, under CAA section 111(b)(1)(A), the source category, as expanded to include transmission and storage sources, for regulation on grounds that it causes or contributes significantly to air pollution which may reasonably be anticipated to endanger public health or welfare. *Id.* Rather, in order to include the transmission and storage segment on the CAA section 111(b)(1)(A) list for regulation, the EPA is required to treat it as a separate source category and determine that in and of itself it causes or contributes significantly to air pollution which may reasonably be anticipated to endanger public health or welfare. The EPA did not make that determination in the course of promulgating the 2016 Rule. 81 FR 35833.

2. Rescission of the NSPS for Sources in Transmission and Storage Segment

A prerequisite for the EPA to promulgate an NSPS applicable to new sources is that the new sources must be in a source category that the EPA has listed under CAA section 111(b)(1). As stated in section V.B.1 of this preamble, the EPA is removing the transmission and storage segment from the source category. Accordingly, the promulgation of NSPS for transmission and storage sources was contrary to law, and as a result, the EPA is also rescinding the standards for both VOC and GHG emissions in the 2012 Rule and the 2016 Rule for emission sources located in the transmission and storage segment. Specifically, we are rescinding the requirements for compressor affected facilities, pneumatic controller affected facilities, storage vessel affected facilities, and the affected facility that is the collection of fugitive emissions components located at a compressor

Industry Using Data Reported Under 40 CFR part 98 Subpart W. April 9, 2020. Included in Docket ID No. EPA–HQ–OAR–2017–0757.

[30] Gathering and boosting is located between well sites and natural gas processing plants in the Oil and Natural Gas Production source category.

[31] U.S. EPA. ''Revised Prioritized List of Source Categories for NSPS Promulgation.'' March 1979. EPA–450/3–79–023.

[32] 38 FR 15406 (May 4, 1973); 39 FR 9315 (March 8, 1974).

[33] 45 FR 83126 (December 12, 1980); 48 FR 37578 (August 18, 1983).

[34] These reports have since been made available for public viewing at *https://www.foiaonline.gov/foiaonline/action/public/submissionDetails?trackingNumber=EPA-HQ-2018-001886&type=request.*

station, where these affected facilities are located downstream of the natural gas processing plant or, if no gas processing plant is present, after the point of custody transfer. To further clarify that the requirements do not apply to these units, we are adding a definition of ''natural gas transmission and storage segment'' which describes the boundaries of the segment. The definitions of ''natural gas processing plant'' and ''custody transfer'' are unchanged.

3. Status of Sources in Transmission and Storage Segment

The result of this final rule, as it relates to the transmission and storage segment, is that these sources are not part of a listed source category under CAA section 111(b)(1)(A) and, thus, are not subject to regulation under CAA section 111(b) (for new sources) or CAA section 111(d) (for existing sources that emit certain air pollutants). This is consistent with the treatment of emissions sources in other industries that the EPA has not listed as a source category under CAA section 111(b)(1)(A). In the future, the EPA may evaluate these emissions more closely and determine whether the transmission and storage segment should be listed as a source category under CAA section 111(b)(1)(A).[35]

4. Rescission of the Limitations on Methane for Sources in the Production and Processing Segments

As the second of the two main actions of this final rule, the EPA is also rescinding the limits on methane emissions for the NSPS applicable to sources in the production and processing segments. The EPA finds that, in the specific circumstances presented here, the EPA erred in establishing the methane NSPS because those requirements are redundant with the NSPS for VOC, establish no additional health protections, and are, thus, unnecessary. Even if the 2016 Rule's establishment of limits on methane emissions is not considered to be, the EPA would exercise its discretion to rescind them on those same grounds. Rescinding the applicability of the 2016 Rule requirements to methane emissions, while maintaining the applicability of those requirements to VOC emissions, will not affect the amount of methane reductions that those requirements will achieve, because the controls that reduce VOC emissions simultaneously reduce methane emissions.

Comments were received on both sides of this proposed decision and the rescission of the requirements for methane and the associated rationale. We respond to some of the major comments in the discussion immediately below and in section VIII.B of this preamble, and to the rest in Chapter 6 of the Response to Comments Document. None of the comments received have led the EPA to materially change its views from the proposal, and as a result, the EPA is rescinding the methane NSPS. The following is the rationale for this decision.

In the 2016 Rule, the EPA justified regulating methane for the following reasons: At the outset, the EPA noted that methane is a GHG, that the EPA has determined that GHG pollution endangers public health and welfare, and that the Crude Oil and Natural Gas Production source category is one of the nation's largest industrial emitters of methane. 81 FR 35825. The EPA also noted that ''[r]educing methane emissions . . . will contribute to efforts to reduce global background ozone concentrations that contribute to the incidence of ozone-related health effects.'' *Id.* at 35837. The EPA went on to determine that the amounts of emissions of methane from the source category were sufficiently large that it was rational to regulate them under CAA section 111, and that, in the alternative, assuming that it was necessary to determine that those emissions cause or contribute significantly to dangerous GHG air pollution, the EPA made that determination as well. *Id.* at 35841–43.

The EPA recognized that the controls that facilities use to meet the VOC NSPS ''also reduce methane emissions incidentally.'' *Id.* at 35841. However, the Agency added that ''in light of the current and projected future GHG emissions from the oil and natural gas industry, reducing GHG emissions from this source category should not be treated simply as an incidental benefit to VOC reduction; rather, it is something that should be directly addressed through GHG standards in the form of limits on methane emissions under CAA section 111(b) based on direct evaluation of the extent and impact of GHG emissions from this source category and the emission reductions that can be achieved through the best system for their reduction.'' *Id.* The Agency added, ''The standards detailed in this final action will achieve meaningful GHG reductions and will be an important step towards mitigating the impact of GHG emissions on climate change.'' *Id.*

The EPA further justified methane requirements by noting that ''there are cost-effective controls that can simultaneously reduce both methane and VOC emissions from these equipment across the industry, and in many instances, they are cost effective even if all the costs are attributed to methane reduction.'' *Id.* In addition, the EPA noted that ''establishing both GHG and VOC standards for equipment across the industry will also promote consistency by providing the same regulatory regime for this equipment throughout the oil and natural gas source category for both VOC and GHG, thereby facilitating implementation and enforcement.'' *Id.* The Agency added that, ''[w]hile this final rule will result in additional reductions [of GHG] . . ., the EPA often revises standards even where the revision will not lead to any additional reductions of a pollutant because another standard regulates a different pollutant using the same control equipment. For example, in 2014, the EPA revised the Kraft Pulp Mill NSPS in 40 CFR part 60 subpart BB published at 70 FR 18952 (April 4, 2014) to align the NSPS standards with the National Emission Standards for Hazardous Air Pollutants (NESHAP) standards for those sources in 40 CFR part 63, subpart S. Although no previously unregulated sources were added to the Kraft Pulp Mill NSPS, several emission limits were adjusted downward. The revised NSPS did not achieve additional reductions beyond those achieved by the NESHAP, but aligning the NSPS with the NESHAP eased the compliance burden for the sources.'' *Id.* n.60.

In *F.C.C.* v. *Fox Television Stations, Inc.,* 556 U.S. 502 (2009), the U.S. Supreme Court described the type of reasoning an agency must provide to justify changing a rule it has previously adopted:

> We find no basis in the Administrative Procedure Act or in our opinions for a requirement that all agency change be subjected to more searching review. The Act mentions no such heightened standard. And our opinion in *Motor Vehicle Mfrs. Assn. of United States, Inc.* v. *State Farm Mut. Automobile Ins. Co.,* 463 U.S. 29 (1983)

[35] Methane emissions from the transmission and storage segment are 34 MMT CO_2 Eq. (1,355 kt methane) per the Inventory of United States Greenhouse Gas Emissions and Sinks: 1990–2018 (published April 13, 2020), which amounts to 5 percent of United States methane emissions and 0.6 percent of total U.S. GHG emissions on a CO_2 equivalent basis (using a GWP of 25 for methane). With respect to VOC emissions, the transmission and storage segment emitted 14 kt in 2017, which amounts to just 5.8 percent of national VOC emissions from that year. With respect to SO_2 emissions, there were 1 kt emitted from the transmission and storage segment in 2017, or just 1.8 percent of national SO_2 emissions. For HAP emissions, the transmission and storage segment emitted 1,143 tons in 2014, or just 0.01 percent of national HAP emissions for that year.

neither held nor implied that every agency action representing a policy change must be justified by reasons more substantial than those required to adopt a policy in the first instance. . . . The statute makes no distinction, however, between initial agency action and subsequent agency action undoing or revising that action.

To be sure, the requirement that an agency provide reasoned explanation for its action would ordinarily demand that it display awareness that it *is* changing position. . . . And of course the agency must show that there are good reasons for the new policy. But it need not demonstrate to a court's satisfaction that the reasons for the new policy are *better* than the reasons for the old one; it suffices that the new policy is permissible under the statute, that there are good reasons for it, and that the agency *believes* it to be better, which the conscious change of course adequately indicates. This means that the agency need not always provide a more detailed justification than what would suffice for a new policy created on a blank slate. Sometimes it must—when, for example, its new policy rests upon factual findings that contradict those which underlay its prior policy; or when its prior policy has engendered serious reliance interests that must be taken into account. *Smiley* v. *Citibank (South Dakota), N. A.,* 517 U.S. 735, 742, 116 S.Ct. 1730, 135 L.Ed.2d 25 (1996). It would be arbitrary or capricious to ignore such matters. In such cases it is not that further justification is demanded by the mere fact of policy change; but that a reasoned explanation is needed for disregarding facts and circumstances that underlay or were engendered by the prior policy.

Id. at 514–16.

In the 2019 Proposal, the EPA acknowledged that in the 2016 Rule, it decided to add methane requirements even though it was aware that the VOC requirements would, by themselves, achieve the same reductions in methane. 84 FR 50259–60 and n.64 (citing 81 FR 35841). However, in that proposal, the EPA nevertheless stated that upon further review, it was proposing that it erred in 2016 by including methane requirements and explained that those requirements were redundant to the VOC requirements. *Id.* The EPA is finalizing this position for several reasons, which meet the requirements of *Fox Television* for reversing the 2016 Rule and rescinding the methane requirements.

In the 2016 Rule, the EPA justified regulating methane on grounds that methane emissions from this source category are great enough to provide a rational basis for regulation in light of the dangers of GHG air pollution and, in fact, if it were necessary, the Agency would determine that those emissions contribute significantly to GHG air pollution. However, in the present action, the EPA is determining that its rational basis finding and alternative SCF in the 2016 Rule were invalid because they included emissions from the transmission and storage segment, as discussed in section VI of this preamble. Accordingly, this basis [36] in the 2016 Rule for regulating methane is invalid.

Considering only the production and processing segments, the 2016 rational basis determination was incorrect because the methane NSPS was redundant on the grounds that it does not achieve any additional methane reductions beyond what sources achieve by implementing the VOC NSPS.[37] The EPA explained its basis for this view at length in the 2019 Proposal, noting that ''for each emission source in the source category subject to the NSPS, the requirements overlap completely.'' 84 FR 50259. The EPA explained that each emission source in the source category emits methane and VOC as co-pollutants through the same emission points and processes. The requirements of the NSPS, including the emission limits, required controls or changes in operations, monitoring, recordkeeping, reporting, and all other requirements, apply to each emission source's emission points and processes and, therefore, to each emission source's methane and VOC emissions, in precisely the same way. The capture and control devices used to meet the NSPS requirements are the same for these co-pollutants and are not selective with respect to either VOC or methane emissions. *Id.* In the proposal, the EPA gave several examples of how the VOC and methane requirements are duplicative of each other. Some examples include the requirements for well affected facilities, pneumatic controllers, pneumatic pumps, and compressors. For each of these emission points, the applicability requirements in NSPS subpart OOOOa are entirely ''pollutant-blind.'' That is, the requirement to control is based on applicability criteria that are not specific to VOC. For example, a pneumatic controller affected facility is a controller operating at a natural gas bleed rate of greater than 6 standard cubic feet per hour (scfh). The ''natural gas'' bleed rate is based on total gas and does not consider the amount of VOC in the gas. In fact, the VOC content could be zero. Similarly, pneumatic pumps are affected facilities if they are ''natural gas driven.'' All reciprocating and wet-sealed compressors, except those at well sites, are affected facilities. Rescission of the methane standards will have no impact on the number of affected facilities that will be subject to the control requirements in NSPS subpart OOOOa. Further, for well completions, pneumatic controllers, reciprocating compressors, and pneumatic pumps at natural gas processing plants, the control requirements are either equipment standards or work practices that do not distinguish between VOC and methane. For pneumatic pumps, the requirement is a 95-percent reduction in ''natural gas emissions.'' Finally, for wet-sealed centrifugal compressors, the requirement is the only one that specifically mentions VOC or methane, as it requires a 95-percent reduction in VOC and methane. However, removal of ''methane'' will not result in any change in methane reduction as the test method required to demonstrate this level of reduction (EPA Method 25A) measures the reduction of total organic carbon, which includes methane.

Thus, after the rescission of the methane standards, there will be no change in the number of affected facilities subject to the rule. There will also be no impact in the methane emission reductions achieved from those sources. While commenters recognized this fact, some raised concerns that in the future, advances in leak measurement technology may result in situations where VOC and methane controls are not redundant. The EPA points out that any future request for an alternative means of emissions limitation must include a demonstration that the alternative identifies emissions for repair that are at least equivalent to the visible emissions observed (and repaired) using optical gas imaging (OGI) with the current levels of sensitivity to methane, especially where the technology speciates emissions. Section VIII.B of this preamble, as well as Chapter 6 of the Response to Comments Document, includes comments and responses on this topic. Because methane reductions occur anyway as a result of the same controls required under the VOC requirements, the benefits of the methane reductions in protecting public health or welfare do not justify regulation of methane under CAA section 111. By the same token, the fact that the controls are cost effective—even, in many cases, when all of the costs are assigned to the methane requirements—does not justify those requirements. Again, the controls, imposed to reduce VOC, would result in the same amount of methane reductions, even without the methane requirements.

Nor can the methane requirements be justified on grounds that their overlap with VOC requirements is a means to

[36] 81 FR 35833.

[37] The same is true for methane reductions that reduce global ozone levels.

promote consistency by providing the same regulatory regime for this equipment throughout the Oil and Natural Gas source category for both VOC and methane, thereby facilitating implementation and enforcement. Although, as noted above, the EPA regulates the same sources/same pollutants at kraft mills under two differing rules, the requirements were established under two different CAA regulatory programs (*i.e.,* under CAA sections 111 and 112) (two different regulatory regimes). The pollutants regulated under CAA section 111(b) for new, modified, or reconstructed emission units at kraft pulp mills are filterable PM and total reduced sulfur compounds. Opacity is regulated to ensure proper operation and maintenance of the electrostatic precipitator used to control PM emissions. Particulate matter emissions and opacity are also regulated under a separate Federal standard, the subpart MM NESHAP for chemical recovery combustion sources at kraft, soda, sulfite, and stand-alone semichemical pulp mills (40 CFR part 63).

It is rational for the EPA to determine that requirements that are redundant to other requirements are not necessary because they do not result in emission reductions beyond what would otherwise occur. As the EPA noted in the 2019 Proposal, the rulemaking to promulgate NSPS for lime manufacturing plants provides another example of the Agency determining not to promulgate a NSPS for an air pollutant, SO_2, on grounds that the emissions were adequately controlled by emissions controls required under a NSPS for another air pollutant, PM. Standards of Performance for New Stationary Sources Lime Manufacturing Plants, 42 FR 22506 (May 3, 1977). Although in that rulemaking, the EPA did not explicitly state that SO_2 controls would have been redundant and, thus, were unnecessary, the Agency's reasoning was fully consistent with that characterization. Specifically, the EPA noted that the controls it was requiring for PM (a baghouse or an electrostatic precipitator) would achieve 85- to 90-percent reductions in SO_2, and that although the EPA could impose further controls to achieve another 7 percent reduction in SO_2, based on the use of a scrubber, the cost would be too high and the environmental benefits too little for that approach to be appropriate. *Id.* at 22507. Accordingly, the EPA prescribed standards for PM but not for SO_2. *Id.* at 22509 (40 CFR 60.342). That is, it appears that the EPA could have promulgated standards for SO_2 that required the same 85- to 90-percent level of control achieved through compliance with the PM standards (and not the additional 7 percent that would have necessitated installation of a scrubber), but the Agency declined to do so. Even though the EPA did not explicitly describe the potential SO_2 NSPS as redundant and, therefore, unnecessary, the fact that it did not promulgate any standards for SO_2 coupled with its explanation that PM controls reduced SO_2 by 85 to 90 percent make clear that the rulemaking serves as a precedent for the present rulemaking and the Agency's present position that the methane NSPS is redundant to the VOC NSPS. By the same token, in the Lime Manufacturing Plants rule, the EPA declined to promulgate NSPS for (1) nitrogen oxides (NO_X) because they are emitted in low concentrations or (2) CO because, among other things, regulation would produce little environmental benefit. *Id.* at 22507. These rationales for not adopting controls for those air pollutants are similar to the redundancy rationale—the essential point in all cases is that any controls would not result in meaningful emission reductions.

In a more recent rulemaking, under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), the EPA also declined to promulgate requirements that it considered to be redundant, and the Court upheld that action. Under 42 U.S.C. 9608(b)(1), the EPA is required to ''promulgate requirements . . . that classes of facilities establish and maintain evidence of financial responsibility consistent with the degree and duration of risk associated with the production, transportation, treatment, storage, or disposal of hazardous substances.'' In 2018, the EPA took an action in which it declined to issue financial responsibility regulations for the hardrock mining industry. Financial Responsibility Requirements Under CERCLA Section 108(b) for Classes of Facilities in the Hardrock Mining Industry (Final Action), 83 FR 7556, 7556 (February 21, 2018). As summarized by the Court, the EPA stated that ''existing federal and state programs as well as modern mining practices reduced the risk that the EPA would be required to use the Superfund to finance response actions at currently active mines.'' *Idaho Conservation League* v. *Wheeler,* 930 F.3d 494, 501 (D.C. Cir. 2019) (citing 83 FR 7556). The Court upheld that determination, stating that 42 U.S.C. 9608(b)(1) ''does not place any obligation on the EPA to issue redundant financial responsibility requirements.'' *Id.* at 504–5.[38] [39]

One commenter cites two Court cases that it asserts support the view that the EPA must regulate a source's emissions of a particular pollutant under CAA section 111 even where the source already controls those emissions because of other legal obligations. In *New York* v. *Reilly,* 969 F.2d 1147, 1153 (D.C. Cir. 1992), the Court rejected the EPA's argument that it need not ban the burning of lead-acid vehicle batteries under the NSPS for municipal waste combustors because the Resource Conservation and Recovery Act precludes the burning of lead-acid batteries. The Court responded that ''the mere existence of other statutory authority which might undergird EPA's final stance is insufficient to justify the omission of the battery ban.'' In *Portland Cement Ass'n* v. *EPA,* 665 F.3d 177, 191 (D.C. Cir. 2011), the Court rejected legal challenges to an NSPS limit for PM that tracked a concurrently issued PM standard adopted under CAA section 112. The Court explained that, ''[a]lthough both the NSPS and NESHAP rulemaking resulted in a PM emissions limit of 0.01 pounds per ton, EPA arrived at that limit using two different mechanisms,'' and added that ''the final rule . . . noted that kilns would have to install fabric filter technology to comply

[38] In addition, as the EPA noted in the 2019 Proposal, it ''ha[s] 'historically declined to propose standards for a pollutant [that] is emit[ted] in low amounts . . . .' '' 80 FR 56599 (quoting 75 FR 54970, 54997 (September 9, 2010). This situation is similar to the present situation in which a pollutant (methane) is fully controlled by requirements applicable to a second pollutant (VOC).

[39] The EPA notes that removing the applicability of the NSPS to methane emissions does not alter the basis for the applicability of the NSPS to VOC emissions for affected sources in the source category, which for some affected sources have been regulated since the 2012 Rule. To determine the best system of emission reduction (BSER), the EPA assesses a set of factors, which include the amount of emissions reduction, costs, energy requirements, non-air quality impacts, and the advancement of particular types of technology or other means of reducing emissions, and retains discretion to weight the factors differently in any case. In the 2016 NSPS subpart OOOOa, the EPA gave primary weight to the amount of emission reductions and cost. The EPA describes this analysis in depth in the 2015 NSPS subpart OOOOa proposal at 80 FR 56618 through 56620 and 80 FR 56625 through 56627. For the source types in the production and processing segments, the NSPS requirements, considered on a VOC-only basis, are cost effective (relatively low cost and relatively high emissions reductions). *See* memorandum titled ''Control Cost and Emission Changes under the Amendments to 40 CFR part 60, subpart OOOOa Under Executive Order 13783,'' in the public docket for this action. The EPA provides this information for the benefit of the public and is not reopening the above-described determination in the 2016 NSPS subpart OOOOa that the VOC-only requirements for sources in the production and processing segments meet the requirements of CAA section 111.

with NESHAP, . . . and the parallel NSPS rule would therefore have no additional cost.'' The commenter states that, similarly, while the EPA set the same BSER for methane and VOC in the 2016 Rule, the considerations underlying the BSER analysis differs significantly for these pollutants, which cause distinct harms. However, these cases are distinguishable because they stand for the proposition that when two separate statutory requirements apply, each must be given effect, and compliance with one does not obviate the other. In the present rulemaking, only one statutory requirement is applicable—the CAA section 111(b)(1)(B) requirement to promulgate standards of performance—and the EPA has determined that promulgating a standard of performance for VOC emissions obviates the need for a standard of performance for methane emissions from the same sources. Further, as the EPA noted in the 2019 Proposal, the EPA has historically declined to propose standards for a pollutant that is emitted in small amounts. 84 FR 50260. In the case of the Oil and Natural Gas Production source category, there are no methane emissions from the sources subject to the NSPS beyond those emissions already subject to control by the provisions to control VOC in the NSPS. Accordingly, there is no need to add NSPS requirements applicable to methane.

The EPA recognizes that in rescinding one set of standards in part for its redundancy with another set, the EPA is choosing to rescind the applicability of those standards to methane emissions and not VOC emissions, rather than vice-versa. Rescinding the methane-specific standards is reasonable because the requirements for VOC and correspondingly, sources' compliance with those requirements, are longer established than those for methane. As described earlier, the EPA regulated VOC first, beginning in 1985 and continuing in 2012, and then added regulation of methane for some sources in 2016.

Additionally, redundancy is not uniform across affected facilities in the production and processing segments. All sources in the segments are subject to VOC requirements and many are subject to methane requirements as well. However, some sources, such as storage vessels, are subject only to VOC requirements and not methane requirements. For those sources, it cannot be said that regulation of VOC is redundant to regulation of methane because the EPA has not regulated methane from them. In addition, there are no sources that are subject to only methane requirements. For these reasons, in choosing between the two requirements, the EPA considers it appropriate and less disruptive to rescind the methane standards.

Commenters asserted that the methane NSPS are not redundant to the VOC NSPS because the former trigger the requirements in CAA section 111(d) to regulate methane from existing sources, but the VOC NSPS do not trigger CAA section 111(d) requirements to regulate VOC from existing sources. The commenters noted that the EPA must consider emissions from existing sources when determining whether to list the source category, which is the predicate to regulating a given pollutant under CAA section 111.

The commenters are correct that methane NSPS, but not VOC NSPS, would trigger the CAA section 111(d) requirements for existing sources,[40] but the fact that the methane NSPS carries with it a trigger for CAA section 111(d) regulation of existing sources is simply a legal consequence of the requirements of CAA section 111, and does not undermine the EPA's conclusion that methane NSPS are redundant. Nor does the fact that the EPA considers emissions from existing sources in listing the source category. These conclusions are supported by the structure of CAA section 111. This provision establishes a multi-step process for regulation. Section 111(b)(1)(A) of the CAA directs the EPA to list source categories for regulation, CAA section 111(b)(1)(B) directs the EPA then to promulgate standards of performance for pollutants emitted from new sources, and CAA section 111(d)(1) directs the EPA then to promulgate guidelines for states to adopt standards of performance for certain of those pollutants emitted by existing sources. As explained above and in responses to comments, the basis for rescinding the applicability of the standards of performance for methane emissions is that those NSPS are redundant with the VOC NSPS. The legal consequence of that rescission is that the EPA is not authorized to promulgate CAA section 111(d) guidelines for existing sources. That consequence does not negate the fact that the methane NSPS is redundant with the VOC NSPS.

As discussed in section VII.B of this preamble, the EPA believes that the impact of not regulating existing oil and natural gas sources under CAA section 111(d) will be limited due to existing factors that encourage or require control of emissions from oil and natural gas existing sources. For comments on that view, and the EPA's response to those comments, see section X.B of this preamble.

Additional comments and responses by the EPA on the rescission of the applicability to methane are provided in section VIII.B of this preamble and in Chapter 6 of the Response to Comments Document.

In the next section, the EPA concludes that the 2016 Rule's determination that methane emissions from the source category contribute significantly to dangerous air pollution was erroneous and must be rescinded. Rescinding that determination also requires rescinding the methane NSPS. The redundancy of the methane requirements and the inadequacy of the 2016 Rule's SCF for methane are separate and independent reasons for rescinding the methane NSPS, and, thus, are severable from each other.

VI. Significant Contribution

The EPA is finalizing the position that the Administrator is required to determine that methane emissions from the Crude Oil and Natural Gas Production source category cause or contribute significantly to GHG air pollution as a predicate for promulgating standards of performance for methane. The EPA solicited comment on this position in the 2019 Proposal, based on an interpretation of section 111 of the CAA, and the EPA bases this final action on a refinement of that interpretation. Specifically, the EPA interprets the requirement of CAA section 111(b)(1)(B) that the Administrator propose to ''establish[ ] . . . standards of performance'' and then finalize ''such standards''—together with the CAA section 111(a)(1) definition of ''standard of performance'' as a ''standard for emissions of air pollutants''—to limit the standards of performance to only those air pollutants that the Administrator determined cause or contribute significantly to dangerous air pollution when listing the source category under CAA section 111(b)(1)(A). If the Administrator did not, when listing the source category, determine that a particular air pollutant causes or contributes significantly to dangerous air pollution, then the Administrator must do so as a predicate to promulgating standards of performance for that air pollutant.

Section VI.A of this preamble, immediately below, discusses that interpretation of CAA section 111. In section VI.B of this preamble, we explain how this interpretation applies

[40] In section VII below, we finalize our proposal that VOC NSPS do not trigger CAA section 111(d) requirements.

to the regulation of methane from the Crude Oil and Natural Gas Production source category. In section VI.C of this preamble, we briefly discuss criteria for making a SCF under CAA section 111.

A. Legal Interpretation Concerning the Air Pollutants That Are Subject to CAA Section 111

1. 2019 Proposal

As noted above, CAA section 111 establishes a process for the EPA to regulate air pollutants from industrial source categories. Section 111(b)(1)(A) of the CAA requires the first step: the Administrator must list a particular category of stationary sources that ''causes, or contributes significantly to, air pollution which may reasonably be anticipated to endanger public health or welfare,'' and then, under CAA section 111(b)(1)(B), the Administrator must proceed to promulgate standards of performance for that source category. For convenience, we refer to ''air pollution which may reasonably be anticipated to endanger public health or welfare'' as dangerous air pollution, and we refer to the reference to ''causes or contributes significantly'' as the SCF. In the 2019 Proposal, we solicited comment on whether CAA section 111(b)(1)(A) must be read, or reasonably could be read, to require the Administrator to make not only a SCF to list the source category, but also a SCF for a particular air pollutant as a predicate to promulgating a standard of performance for that pollutant under CAA section 111(b)(1)(B).

The EPA supported this interpretation with a detailed discussion of the relevant statutory provisions, their context, and purpose, as well as past administrative practice. At the outset, the EPA acknowledged that CAA section 111(b)(1)(A) by its terms requires that the Administrator make a SCF for the source category, and is silent on individual air pollutants.[41] However, the EPA noted that CAA section 111(b)(1)(A) should be read in conjunction with CAA sections 111(b)(1)(B) and 111(a)(1), which require the Administrator to promulgate ''standards of performance,'' defined as ''standard[s] for emissions of air pollutants.'' The EPA posited that those provisions, read together, by virtue of their focus on emissions of air pollutants, could be interpreted to require or authorize the EPA to require a pollutant-specific SCF as a predicate for promulgating a standard of performance. 84 FR 50263. The EPA acknowledged that in the past it has not promulgated a pollutant-specific SCF, and instead has taken the position that it may promulgate a standard of performance for a pollutant not previously regulated under CAA section 111 as long as it simply has a rational basis for doing so. In the 2019 Proposal, the EPA explained that this approach is flawed because it is vague and not guided by any statutory criteria, and that as a result, it could result in the Agency promulgating standards for air pollutants that are emitted in relatively minor amounts. 84 FR 50263. The Agency stated that interpreting CAA section 111 to require a pollutant-specific SCF as a predicate to regulating the pollutant would guard against this possibility.[42]

2. Comments

The EPA received comment on all aspects of its solicitation of comment. Some commenters supported the EPA's arguments and urged the Agency to finalize an interpretation that requires the Administrator to make a pollutant-specific SCF as a predicate to promulgating standards of performance for that pollutant from a source category. Other commenters opposed this interpretation and sought to counter the support for it that the EPA offered. They argued that under CAA section 111(b)(1)(A), the SCF applies only to source categories. They further argued that the references in CAA sections 111(b)(1)(B) and 111(a)(1) to air pollutants are unremarkable because standards of performance necessarily apply to particular air pollutants, and should not be read to elucidate the meaning of CAA section 111(b)(1)(A) in the manner the EPA suggested.[43] These comments are discussed in more detail in section IX of this preamble and in Chapter 8 of the Response to Comments Document located in the docket for this rulemaking.

3. Final Action

The EPA is finalizing the position that CAA section 111 requires, or at least authorizes the Administrator to require a pollutant-specific SCF as a predicate for promulgating a standard of performance for that air pollutant. The EPA bases this position primarily on a refinement of the interpretation of CAA section 111, described above, on which it solicited comment. Specifically, the EPA interprets the CAA section 111(b)(1)(B) requirement that the Administrator propose to ''establish[ ] . . . standards of performance'' and then finalize ''such standards with such modifications as he deems appropriate,'' in light of both the CAA section 111(a)(1) definition of ''standard of performance'' as a ''standard for emissions of air pollutants,'' and CAA section 111(b)(1)(A), which requires the Administrator to list a source category only ''if in his judgment it causes, or contributes significantly to [dangerous] air pollution.'' Read in this context, CAA section 111(b)(1)(B) is best understood *not* to require the Administrator to promulgate standards for emissions of *all* air pollutants but only to require him or her to promulgate standards for the emissions of air pollutants that the Administrator has determined ''cause or contribute significantly'' to the ''air pollution'' that the Administrator determined to be dangerous when listing the source category. Under this interpretation, if the Administrator did not, in listing the source category, determine that a particular air pollutant causes or contributes significantly to the dangerous air pollution, section 111 requires the Administrator to make—or, at least, authorizes the Administrator to require—a pollutant-specific SCF as a predicate to regulating that air pollutant.[44]

[41] It should be noted that even though CAA section 111(b)(1)(A) is clear in requiring a SCF for the source category, its silence as to individual air pollutants, which of course are what causes or contributes significantly to dangerous air pollution and are the subject of regulation, leaves to the EPA the task of addressing individual air pollutants.

[42] The EPA went on to review other provisions in the CAA that explicitly require a pollutant-specific SCF; the legislative history accompanying these provisions; the references in another CAA section 111 provision, CAA section 111(f)(2)(A) and (B), to the impacts of particular pollutants on dangerous air pollution; and previous interpretations that the EPA had made of the CAA section 111 requirements concerning individual air pollutants. 84 FR 50263–67.

[43] The commenters objected to the EPA's interpretation of other CAA provisions, of legislative history, and of other provisions of CAA section 111, as well as the EPA's interpretations of CAA section 111 in earlier administrative actions. We discuss these comments in the Response to Comments Document located in the public docket of this final rulemaking.

[44] Although this interpretation is a refinement of the interpretation for which the EPA solicited comment in the 2019 Proposal, it is rooted in the Proposal. As noted in the summary above, in supporting the interpretation that CAA section 111(b)(1)(A) requires or authorizes the EPA to require a pollutant-specific SCF, the EPA made numerous references to CAA sections 111(a)(1) and 111(b)(1)(B), and made clear that those three provisions must be read together. The EPA made other references as well to the need to make a pollutant-specific SCF in order to promulgate standards of performance, which is the thrust of the interpretation described in this final action. *See Id.* at 50262–63. The rational basis approach was an interpretation of CAA section 111(b)(1)(B). That is, under this approach, the EPA interpreted that provision to authorize standards of performance for those air pollutants for which the EPA had a rational basis, but not necessarily standards for all air pollutants. *See* 81 FR 35842 (2016 Rule), *cited*

4. Legal Interpretation of CAA Sections 111(a)(1), (b)(1)(B), and (b)(1)(A) and the Pollutants Subject to Regulation

The EPA interprets CAA sections 111(b)(1)(B), in light of CAA sections (b)(1)(A) and (a)(1), to require, or at least to authorize the Administrator to require, a pollutant-specific SCF as a predicate for promulgating a standard of performance for that air pollutant. The EPA bases this interpretation on a close reading of these provisions in the context of CAA section 111. CAA section 111 directs the EPA to regulate, through a multi-step process, air pollutants from categories of stationary sources. CAA section 111(b)(1)(A) requires the initial action, which is that the Administrator must ''publish . . . a list of categories of stationary sources. He shall include a category of sources in such list if in his judgment it causes, or contributes significantly to, air pollution which may reasonably be anticipated to endanger public health or welfare.'' This provision does not by its terms require the Administrator, in listing a source category, to identify particular air pollutants of concern that are emitted from the source category, but it does make clear that the Administrator must identify air pollution that is of concern and must make a finding that this air pollution, in our shorthand, is dangerous.

CAA section 111(b)(1)(B) then directs the EPA to propose regulations ''establishing Federal standards of performance'' for new sources within the source category, then to allow public comment, and then to ''promulgate . . . such standards with such modifications as he deems appropriate.'' CAA section 111(a)(1) defines the term ''standard of performance'' as ''a standard for emissions of air pollutants which [the Administrator is required to determine through a specified methodology].'' This definition makes clear that the standards of performance that CAA section 111(b)(1)(A) directs the Administrator to promulgate must concern air pollutants emitted from the sources in the source category. However, industrial sources of the type subject to CAA section 111(b)(1)(A) invariably emit more than one air pollutant and neither CAA section 111(b)(1)(B) nor 111(a)(1) by its terms specifies for which of those air pollutants the EPA must promulgate standards of performance.

But the statute does provide guidance as to the class of air pollutants for which the EPA must promulgate standards of performance. Section 111(b)(1)(A) of the CAA demonstrates that the statutory scheme of CAA section 111 is aimed at controlling ''air pollution which may reasonably be anticipated to endanger public health or welfare.'' It follows that the air pollutants for which the Administrator must establish standards must, or at least may reasonably, be limited to those air pollutants which contribute to this dangerous air pollution.

The Administrator's discretion to limit the class of air pollutants for which he promulgates standards is supported by his statutory discretion under CAA section 111(b)(1)(B) to finalize standards ''with such modifications as he deems appropriate.'' In an exercise of this discretion, the Administrator deems it appropriate to limit the standards of performance to those air pollutants that contribute to dangerous air pollution.

Several other provisions in CAA section 111 also refer to air pollutants, including CAA section 111(b)(3), which requires the Administrator to, ''from time to time, issue information on pollution control techniques for categories of new sources and air pollutants subject to the provisions of this section.'' This reference to ''air pollutants *subject to the provisions of this section*'' (emphasis added) implies that some air pollutants may not be subject to CAA section 111; otherwise, the emphasized phrase would be superfluous.[45]

As noted in the 2019 Proposal, in the past, the EPA has interpreted CAA section 111(b)(1)(B) to authorize it to promulgate standards of performance for any air pollutant that the EPA identified in listing the source category and any additional air pollutant for which the EPA has identified a rational basis for regulation. 81 FR 35843 (2016 Oil & Gas Methane Rule); ''Standards of Performance for Greenhouse Gas Emissions from New, Modified, and Reconstructed Stationary Sources: Electric Utility Generating Units—Final Rule,'' 80 FR 64510 (October 23, 2015) (EGU CO_2 NSPS Rule). Inherent in this approach is the recognition that CAA section 111(b)(1)(A) does not, by its terms, necessarily require the EPA to promulgate standards of performance for all air pollutants emitting from the source category. Citizen group stakeholders and some states have endorsed the rational basis approach. Some industry stakeholders and other states, however, have advocated a narrower approach with respect to, at least, the GHG for which the EPA promulgated standards of performance for the Fossil Fuel-Fired Electric Utility Generating Units source category and the Crude Oil and Natural Gas Production source category. The stakeholders argued that under this narrower approach, the EPA is not authorized to promulgate NSPS for at least GHG unless it first makes a SCF with respect to that pollutant.

The EPA interprets the phrase at issue in CAA section 111(b)(1)(B), ''standards of performance,'' and the associated phrase in CAA section 111(a)(1), ''emissions of air pollutants,'' by analogy to the similar phrase, ''any air pollutant,'' found in the CAA permitting provisions that the U.S. Supreme Court considered in *Utility Air Regulatory Group* v. *EPA,* 573 U.S. 302 (2014) (*UARG*). In *UARG,* the Court interpreted CAA section 169(1), which provides construction and modification permitting requirements under the Prevention of Significant Deterioration (PSD) program, and CAA sections 501(2)(B) and 302(j), which provide the operating permit requirements of the title V program. The Court concluded that when read in the context of the permitting provisions, the phrase ''any air pollutant'' did not encompass GHG, even though they are air pollutants. The EPA considers that the analytical approach that the Court adopted in *UARG* also applies to CAA section 111(b)(1)(B). Under this approach, the provisions in that section that direct the Administrator to establish ''standards of performance'' for new sources in the source category, require, or at least reasonably allow, the Administrator to promulgate standards for only those air pollutants for which the EPA has made a SCF.

The EPA considers the same analytical approach to support interpreting ''emissions of air pollutants'' in CAA section 111(a)(1) to encompass only those air pollutants for which the EPA has made a SCF. Under the PSD requirements, no ''major emitting facility'' may be constructed or

in 84 FR 50262 (2019 Proposal). This approach is similar to the pollutant-specific SCF approach. By the same token, the EPA's discussions in the 2019 Proposal of the legislative history, CAA section 111(f), and previous statements the EPA made in support documents all contain references to a pollutant-specific SCF as a predicate for promulgating standards of performance. 84 FR 50263 through 67.

[45] Similarly, CAA section 111(d)(1)(A) makes clear by its terms that ''a standard of performance under this section'' need not govern *all* pollutants emitted from a regulated source to give effect to Congress's purpose. The requirements of CAA section 111(d)(1)(A) apply to only a subset of air pollutants, that is, ''any air pollutant . . . for which air quality criteria have not been issued or which is not included on a list published under section 7408(a) of this title or emitted from a source category which is regulated under section 7412 of this title but . . . to which a standard of performance under this section would apply if such existing source were a new source.''

modified in certain areas of the U.S. unless it has received a permit that includes certain conditions and emission limits. CAA section 165(a)(1). In the PSD definitional provisions, CAA section 169(1) defines the term ''major emitting facility'' as any stationary source of air pollutants that emits, or has the potential to emit, at least 100 or 250 tpy (depending on the source) of ''any air pollutant.'' *See* CAA sections 169(2)(C), 111(a)(4) (defining ''construction'' to include ''modification,'' which in turn is defined to mean, in relevant part, a certain type of change that increases the amount of ''any air pollutant'' emitted by the source). Title V makes it unlawful to operate a ''major source'' without an operating permit that includes all applicable CAA requirements. Title V defines a ''major source'' by incorporating the CAA-wide definition of ''major stationary source:'' A stationary source that emits or has the potential to emit at least 100 tons per year of ''any air pollutant.'' CAA section 501(2)(B), 302(j).

In a 2010 rule, ''Prevention of Significant Deterioration and Title V Greenhouse Gas Tailoring Rule,'' 75 FR 31514 (June 3, 2010) (Tailoring Rule), the EPA took the position that the phrase ''any air pollutant'' in these provisions necessarily included GHG, based on the 2007 decision by the U.S. Supreme Court that the CAA-wide definition of ''air pollutant,'' CAA section 302(g), encompasses GHG. *Massachusetts* v. *EPA,* 549 U.S. 497 (2007). The EPA's interpretation, however, created practical problems, which the Agency recognized in the Tailoring Rule: It would cause numerous commercial and small industrial sources to become subject to the permitting requirements, which were burdensome and which Congress designed to apply only to large industrial sources that were equipped to carry those burdens. *UARG,* 573 U.S. at 310–11 (citing 73 FR 44355, 44498 and 99).

UARG held that the EPA's interpretation of the PSD and title V provisions was unreasonable, and that the phrase ''any air pollutant'' in these provisions did not include GHG. The Court adopted a two-step analysis. First, the Court found that the fact that the CAA-wide definition of ''air pollutant'' included GHG did not mean that all the references to ''air pollutant'' in the CAA's operative provisions necessarily include GHG; rather, whether the term included GHG was dependent on the context of the particular operative provision. 573 U.S. at 316. The Court found support for this position in the fact that ''where the term 'air pollutant' appears in the Act's operative provisions, EPA has routinely given it a narrower, context-appropriate meaning.'' *Id.* The Court explained that the EPA had already interpreted ''any air pollutant'' in the permitting provisions to be limited to ''regulated'' air pollutants, which the Court described as ''a reasonable, context-appropriate meaning.'' *Id.* at 316–17. The Court identified several other provisions ''where EPA has inferred from statutory context that a generic reference to air pollutants does not encompass every substance falling within the Act-wide definition.'' For example, and of particular significance here, the Court noted that CAA section 111(a)(4), read together with CAA sections 111(a)(2) and (b)(1)(B), applies NSPS requirements to a source that undergoes a physical or operational change that increases its emission of ''any air pollutant,'' but the EPA interprets this provision as limited to air pollutants for which the EPA has promulgated standards of performance. 573 U.S. at 317. Similarly, the Court noted that CAA sections 169A(b)(2)(A) and (g)(7) require a certain type of source that interferes with visibility to retrofit if it has the potential to emit 250 tpy of ''any pollutant,'' but that the EPA interprets this provision as limited to visibility-impairing air pollutants. 573 U.S. at 318. The Court emphasized that *Massachusetts* did not call these interpretations into question; rather, according to the Court, ''*Massachusetts* does not foreclose the Agency's use of statutory context to infer that certain of the Act's provisions use 'air pollutant' to denote not every conceivable airborne substance, but only those that may sensibly be encompassed within the particular regulatory program.'' 573 U.S. at 319. Therefore, in this first step, the Court concluded that the CAA did not compel the EPA to interpret the phrase ''any air pollutant'' in the permitting provisions to include GHG.

Second, the Court found that the EPA did not have the discretion to interpret this phrase to include GHG, because it was unreasonable to do so in light of the permitting provisions. The Court explained that including GHG would expand the permitting programs to large numbers of small sources, but that ''a brief review of the relevant statutory provisions leaves no doubt that the PSD program and Title V are designed to apply to, and cannot rationally be extended beyond, a relative handful of large sources capable of shouldering heavy substantive and procedural burdens.'' *Id.* at 322. The Court went on to describe the various PSD and title V statutory requirements that are resource-intensive and time-consuming, and, therefore, incompatible with application to large numbers of small sources. *Id.* at 322–23.

The EPA is adopting *UARG's* two-step analytical approach to conclude that, in light of its context, CAA section 111(b)(1)(B) does not mandate, and cannot reasonably be read to authorize, the EPA to promulgate standards of performance for an air pollutant for which the EPA has not made a SCF. At a minimum, even if these provisions are not read to preclude the EPA from promulgating standards of performance without first making a pollutant-specific SCF, it is reasonable to interpret these provisions as authorizing the EPA to decline to promulgate standards without first making such a SCF. *UARG* was explicit that provisions of CAA section 111 are subject to its analytical approach. As noted above, the Court endorsed the EPA's interpretation that, notwithstanding the reference to ''any air pollutant'' in CAA section 111(a)(4), the requirements concerning a ''modification'' in CAA section 111(b)(1)(B), which is at issue here, and CAA sections 111(a)(2) and (4) do not require the EPA to promulgate standards for every pollutant that a modified source emits, because those provisions must be understood in context to embrace a limited set of air pollutants. 573 U.S. at 317.

As is clear from the EPA's summary above of the CAA section 111 rulemaking process, the first action that the EPA must take, specified in CAA section 111(b)(1)(A), is to list a source category for regulation on the basis of a determination that the category contributes significantly to dangerous air pollution, and it is this provision that establishes the context that is relevant for present purposes. This provision makes clear that although Congress designed CAA section 111 to apply broadly to source categories of all types wherever located, Congress also imposed a constraint: The EPA is authorized to regulate only sources that it finds cause or contribute significantly to air pollution that the EPA finds to be dangerous.

Congress' direction to EPA to promulgate standards of performance for the sources in the category, under CAA section 111(b)(1)(B), must be viewed in this context. Congress did not specify which air pollutants the standards of performance must address, stating only, as noted above, in the definitional provisions of CAA section 111 that the term ''standard of performance'' means a standard for ''emissions of air pollutants.'' This phrase is substantially similar to the phrase ''any air pollutant'' in the PSD and Title V provisions addressed in *UARG.* In fact, ''emissions of air pollutants'' appears to be less encompassing than ''any air pollutant.'' As the U.S. Supreme Court has noted, ''Read naturally, the word 'any' has an expansive meaning, that is, 'one or some indiscriminately of whatever kind.' Webster's Third New International Dictionary 97 (1976).'' *United States* v. *Gonzales,* 520 U.S. 1, 4, 1997), *quoted in Department of Housing and Urban Development* v. *Rucker,* 535 U.S. 125, 131 (2002), *cited in Massachusetts,* 549 U.S. at 529 n.25.

Under the analytical approach of *UARG,* because the regulatory scope of the CAA's ''operative provisions,'' such as CAA sections 111(b)(1)(B) and 111(a)(1), must be understood in context, their reference to ''standards of performance'' and ''emissions of air pollutants'' cannot be read to mandate promulgation of standards of performance for each and every air pollutant emitted from the source category. In addition, because Congress limited the EPA to regulating only stationary sources in a category that the Administrator must first determine to cause or contribute significantly to dangerous air pollution, it is not reasonable to read ''air pollutants'' to refer to any of the source category's air pollutants for which the EPA has not made a SCF. At the very least, it is reasonable to interpret that phrase more narrowly. As noted in the 2019 Proposal, interpreting the CAA section 111 provisions to authorize the EPA to regulate any air pollutant, even ones that the EPA did not consider in listing the source category, creates the risk that the EPA may regulate air pollutants emitted in small quantities or otherwise having little adverse effect.[46]

It is true that, recently, the EPA has adopted the approach of regulating additional air pollutants that it did not address in the listing determination only after determining that it has a rational basis for doing so, and in making that determination, has considered the same factors as it would in making a SCF. 81 FR 35843 (2016 Rule). However, this approach is a creature of Agency practice and, therefore, is not as firmly established as statutory requirements. As noted in the 2019 Proposal, interpreting CAA section 111 to require only a pollutant-specific rational basis standard, and not a SCF, could lead to potentially anomalous results when the Agency, after listing a source category on grounds that its emissions taken together contribute significantly to dangerous air pollution, proceeds to promulgate NSPS for individual air pollutants. EPA stated that, as an example, under the rational basis interpretation, the EPA could list a source category on grounds that it emits numerous air pollutants that, taken together, significantly contribute to air pollution that may reasonably be anticipated to endanger public health or welfare, and proceed to regulate each of those pollutants, without ever finding that each (or any) of those air pollutants by itself causes or contributes significantly to—or, in terms of the text of other provisions, causes or contributes to—air pollution that may reasonably be anticipated to endanger public health or welfare. 84 FR 50263. As further noted in the 2019 Proposal, CAA section 111(b)(1)(A) does not provide or suggest any criteria to define the rational basis approach, the EPA has not articulated any criteria in its previous applications in the EGU CO_2 NSPS and the 2016 subpart OOOOa rules, and in instances before those rules in which the EPA has relied on the ''rational basis'' approach, the EPA has done so to justify not setting a standard for a given pollutant, rather than to justify setting such a standard. *Id.* Thus, the rational basis test allows the EPA virtually unfettered discretion in determining which air pollutants to regulate. As a result, the rational basis standard creates the possibility that the EPA could seek to promulgate NSPS for pollutants that may be emitted in relatively minor amounts, as the EPA noted in the 2019 Proposal. 84 FR 50263. As noted in section IX below, numerous commenters reiterated these concerns.

In contrast, CAA section 111(b)(1)(A) is clear that the EPA may list a source category for regulation only if the EPA determines that the source category ''causes or contributes *significantly*'' (emphasis added) to dangerous air pollution. In light of the stringency of this statutory requirement for listing a source category, it would be unreasonable to interpret CAA section 111(b)(1)(B) to allow the Agency to regulate air pollutants from the source category merely by making an administrative determination under the open-ended and undefined rational basis test. Rather, it is logical to interpret CAA section 111(b)(1)(B) to require that the Agency apply the same degree of rigor in determining which air pollutants to regulate as it does in determining which source categories to list for regulation.

For these reasons, the EPA concludes that in the context of CAA section 111, the requirement that the EPA promulgate ''standards of performance,'' (CAA section 111(b)(1)(B)), defined as ''standard[s] for emissions of air pollutants'' (CAA section 111(a)(1)), must be interpreted to require a pollutant-specific SCF (CAA section 111(b)(1)(A)) as a predicate for promulgating standards of performance. At a minimum, the Agency considers this interpretation to be reasonable and, accordingly, adopts it. Requiring a pollutant-specific SCF establishes a clearer framework for assessing which air pollutants merit regulatory attention that will require sources to bear control costs. This promotes regulatory certainty for stakeholders and consistency in the EPA's identification of which air pollutants to regulate and reduces the risk that air pollutants that do not merit regulation will nevertheless become subject to regulation due to an unduly vague standard.

In the 2019 Proposal, the EPA solicited comment on whether to interpret CAA section 111(b)(1)(A) to require a determination that the pollutant causes or contributes significantly to dangerous air pollution (the SCF) or instead, to interpret it to require a determination that the pollutant simply causes or contributes to dangerous air pollution. 84 FR 50261. The same issue arises with respect to CAA sections 111(b)(1)(B) and (a)(1), but the EPA has concluded that interpreting these provisions to require a SCF as the pollutant-specific finding is consistent with the source-category SCF in CAA section 111(b)(1)(A). That is, in light of Congress' clearly expressed intent in CAA section 111(b)(1)(A) that the EPA base its listing of a source category on a finding that the emissions from the source category contribute significantly to dangerous air pollution, the EPA concludes that CAA sections 111(b)(1)(B) and (a)(1) require the EPA to base its regulation of a pollutant on a similarly rigorous finding that the pollutant contributes significantly to dangerous air pollution. If, in the alternative, the statute is ambiguous in this regard, the EPA exercises its

[46] As should be clear from this discussion immediately above, this interpretation of CAA sections 111(b)(1)(B) and (a)(1) differ from the interpretation of CAA section 111(b)(1)(A) that the EPA described in the 2019 Proposal. *See* 84 FR 50263 (stating that interpreting CAA section 111(b)(1)(B), the EPA was mindful that an Agency ''[may] avoid a literal interpretation at Chevron step one . . . [by] show[ing] either that, as a matter of historical fact, Congress did not mean what it appears to have said, or that, as a matter of logic and statutory structure, it almost surely could not have meant it'' (citation omitted)).

discretion to interpret it to require a pollutant-specific SCF.

In the 2019 Proposal, the EPA noted that interpreting CAA section 111 to require a pollutant-specific SCF as a predicate to regulation ''need not result in duplicative SCFs (or duplicative associated endangerment findings). That is, the EPA would not need to make separate SCFs (and associated endangerment findings) for both the source category and each pollutant emitted by the source category that the EPA seeks to regulate.'' 84 FR 50266. The EPA continues to hold this view. In identifying any new source categories under CAA section 111(b)(1)(A), the EPA could identify each air pollutant of concern and make a SCF, as appropriate, for emissions of each of those pollutants from the source category, and, in that same action, make the SCF for the source category itself. In addition, in the 2019 Proposal, the EPA solicited comment on what implications interpreting CAA section 111 to require a pollutant-specific SCF would give rise to for already promulgated standards of performance. *Id.* The EPA believes that standards of performance will generally not be affected by this requirement because generally, the EPA identified and analyzed the air pollutants of concern when the EPA listed a source category, or initiated promulgation of standards of performance at the same time or shortly after listing the source category, and, therefore, in association with the significance determination the Agency made in that listing. For example, as noted elsewhere, the EPA followed that process when it listed the Crude Oil and Natural Gas Production source category, that is, it identified and analyzed the air pollutants of concern at that time in the supporting documents. Importantly, the EPA relied on its analyses of those air pollutants as the basis for determining that the source categories' emissions contribute significantly to dangerous air pollution.[47]

B. Flaws in the 2016 Rule's Significant Contribution Finding

When the Administrator listed the oil and natural gas industry as a source category in 1979, he did not determine that methane emissions from the source category cause or contribute significantly to dangerous air pollution. In this rulemaking, the EPA is taking the position that the EPA must make that determination as a predicate to promulgating standards of performance for methane from this source category. The Administrator did determine in the 2016 Rule that methane from the source category contributes significantly to dangerous air pollution, but that determination was flawed and must be rescinded for two reasons: (1) The Administrator made that determination on the basis of methane emissions from the production, processing, and transmission and storage segments, instead of just the production and processing segments; and (2) the Administrator failed to support that determination with either established criteria or some type of reasonably explained and intelligible standard or threshold for determining when an air pollutant contributes significantly to dangerous air pollution.

1. Improper Scope of Source Category

In the 2016 Rule, the Administrator made the significant contribution finding on the basis of assessing methane emissions from the source category as defined to include the production, processing, and transmission and storage segments. In the present action, we are removing the transmission and storage segment, leaving only the production and processing segments. Because the 2016 Rule did not assess whether methane emissions from the production and processing segments alone cause or contribute significantly to dangerous air pollution, we find that the Rule's determination is not adequate and, therefore, we are rescinding it. Until the EPA makes an appropriate determination that methane emissions from the Oil and Natural Gas source category, properly calculated, contribute significantly to dangerous air pollution, it does not have authority to promulgate standards of performance for methane from these sources under CAA section 111(b)(1)(b).

2. Lack of Criteria or Standard for Determining Significant Contribution

In the 2019 Proposal, the EPA ''solicit[ed] comment on the question of whether the SCF in the 2016 . . . [R]ule can be considered appropriate given that nowhere in the course of developing and promulgating that rule did the EPA set forth the standard by which the 'significance' of the contribution of the methane emissions from the source category (as revised) was to be assessed.'' 84 FR 50267. The EPA elaborated that it was asking for comment on whether, as a matter of law, under CAA section 111, the EPA is obligated to identify the standard by which it determines whether a source category's emissions ''contribute significantly,'' and whether, if not so obligated, the EPA nevertheless fails to engage in reasoned decision-making by not identifying that standard. *Id.* The EPA cited *Motor Vehicle Mfrs. Assn. of United States, Inc.* v. *State Farm Mut. Automobile Ins. Co.,* 463 U.S. 29, 43 (1983), which states, ''Normally, an agency rule would be arbitrary and capricious if the agency has . . . entirely failed to consider an important aspect of the problem.''. *Id. See Department of Homeland Security* v. *Regents of Univ. of Cal.,* No. 18–587, slip op. at 18 (U.S. June 18, 2020) (executive action to rescind the Deferred Action for Childhood Arrivals program failed to provide a reasoned explanation when it failed to consider certain ''conspicuous issues''). For the reasons that follow, the EPA concludes that the failure to identify any such standard or any established set of criteria for the 2016 Rule's SCF for methane emissions from the source category is unreasonable and requires rescinding the 2016 Rule's SCF.

As the EPA noted in the 2019 Proposal, the ''contributes significantly'' provision in CAA section 111(b)(1)(A) is ambiguous. *See* 84 FR 50267–68 (citing *EPA* v. *EME Homer City Generation, L.P.,* 572 U.S. 489 (2014) (holding that a similar provision in CAA section 110(a)(2)(D)(i), often termed the ''good neighbor'' provision, is ambiguous)). Accordingly, the EPA has authority to interpret that provision. *Id.* at 50268. As noted above, the EPA reads CAA section 111(b)(1)(B) in light of CAA sections 111(b)(1)(A) and (a)(1) to incorporate the ''contributes significantly'' standard in connection with promulgating NSPS for particular air pollutants. The EPA has concluded that to allow the EPA to distinguish between a *contribution* and a *significant contribution* to dangerous pollution, some type of (reasonably explained and intelligible) standard and/or established set of criteria that can be consistently applied is necessary. Without at least one or the other, it is impossible to evaluate whether the SCF is well reasoned. Therefore, the lack of a standard or established set of criteria for the 2016 Rule's SCF renders the finding arbitrary and capricious. A supporting basis for this conclusion can be found in the EPA's analysis of the ''contribute significantly'' provisions of CAA section 189(e), concerning major stationary sources of PM with a diameter of 10 micrometers or less (PM_{10}). This provision requires that the

[47] The EPA also took the approach in the 2016 Rule that it is revising here, when it attempted to expand the Crude Oil and Natural Gas Production source category. It discussed the pollutant emissions, including GHG, VOC, and SO_2, made a SCF for those emissions, and, on the basis of that SCF, listed the expanded source category. 81 FR 35837 through 40.

control requirements applicable to major stationary sources of PM_{10} also apply to major stationary sources of PM_{10} precursors ''except where the Administrator determines that such sources [of precursors] do not contribute significantly to PM_{10} levels which exceed the standard in the area.'' As the EPA noted in the 2019 Proposal, in CAA section 189(e), Congress intended that, in order to be subject to regulation, the emissions must have a greater impact than a simple contribution not characterized as a significant contribution. However, Congress did not quantify how much greater. Therefore, the EPA developed criteria for identifying whether the impact of a particular precursor would ''contribute significantly'' to a NAAQS exceedance. 84 FR 50268. These criteria included numerical thresholds. *Id.*

The EPA has concluded similarly that, under CAA section 111(b), a standard or an established set of a criteria, or perhaps both, are necessary to identify what is significant and what is not. Moreover, without either, any determination of significance is arbitrary and capricious because it does not identify a reasoned basis for that determination.[48] This is evident in the flawed significance finding in the 2016 Rule. There, the EPA determined that ''the collective GHG emissions from the oil and natural gas source category are significant'' and based that determination on several facts concerning the amount of methane emissions from the Oil and Gas source category, in comparison to other domestic and global emissions. Specifically, the EPA stated that oil and gas GHG emissions are significant, whether the comparison is (i) ''domestic'' (noting that this sector is ''the largest source of methane emissions, accounting for 32 percent of United States methane and 3.4 percent of total United States emissions of all GHG''), (ii) ''global'' (noting that this sector, ''while accounting for 0.5 percent of all global GHG emissions, emits more than the total national emissions of over 150 countries, and combined emissions of over 50 countries''), or (iii) ''when both the domestic and global GHG emissions comparisons are viewed in combination.'' 81 FR 35840. The EPA did add a qualitative assessment of those facts. It noted that ''no single GHG source category dominates on the global scale,'' noted further that the oil and natural gas source category, ''like many (if not all) individual GHG source categories, could appear small in comparison to total emissions,'' and asserted that nevertheless, ''in fact, it is a very important contributor in terms of both absolute emissions, and in comparison to other source categories globally or within the United States.'' *Id.* However, the EPA did not identify any set of criteria by which to evaluate those facts and to ensure that those facts constituted the comprehensive set of data for determining significance. In contrast, when the EPA determines whether an area should be designated nonattainment on grounds that it ''contributes'' to ambient air quality problems in a nearby area, the EPA applies an established set of criteria that identify the relevant sets of data to analyze and explain how to analyze them. *See Catawba Cty.* v. *EPA,* 571 F.3d 20, 39–40 (DC Cir. 2009) (*Catawba*) (holding that in determining whether an area ''contributes'' to downwind ozone air quality problems, the EPA, ''[t]o be reasonable . . . must . . . define and explain the criteria the agency is applying''; explaining that the EPA adopted a set of nine criteria that it defined and explained ''in spades''). These criteria help ensure that the EPA's decision-making is well-reasoned and consistent. The EPA considers it particularly important to develop a set of criteria and/or a standard in order to determine when a *significant* contribution occurs, in order, as noted above, to distinguish it from a simple contribution. A contribution can be greater or lesser and remain a contribution, but a significant contribution determination necessarily involves a judgment about the degree of the contribution that rises to the level of significance. For such a judgment to be meaningful (and to be understood by regulated parties and by the public), the Agency must identify the criteria it will use to determine significance. In the 2016 Rule's significance finding, the EPA did not identify such criteria.

Nor did the EPA identify any threshold against which to compare the cited facts concerning methane emissions, and thereby assess their importance, much less explain why a contribution above such a threshold should be deemed significant while a contribution below it should not. Thus, for example, although the EPA justified the significance determination, in part, on grounds that the source category's emissions constitute 3.4 percent of total U.S. GHG emissions and 0.5 percent of all global GHG emissions, the EPA did not explain why either of those facts supports the significance determination. Because the EPA did not identify a threshold or criteria for evaluating the oil and gas industry's percentage of domestic or global GHG emissions, the EPA could not justify the 2016 Rule's SCF. As a result, that determination cannot be considered the result of reasoned and appropriate decision-making.[49] The EPA intends to begin

[48] As noted in the 2019 Proposal, in a 1994 rule concerning CAA section 213(a), which requires the EPA to make a finding that air pollutant emissions from new and existing nonroad engines and vehicles are ''significant contributors'' to dangerous air pollution, the EPA determined that it is not necessary to establish a ''specific numerical standard'' for determining significance. 84 FR 50268 (citing 59 FR 31306 and 31308 (June 17, 1994)). However, more recently, as further noted in the 2019 Proposal, the EPA promulgated criteria to interpret and apply ''contribute significantly'' in the ''good neighbor'' provision, CAA section 110(a)(2)(D)(i). 84 FR 50267 and 68 (discussing the criteria and the EPA's use of them in the Cross State Air Pollution Rule, which the U.S. Supreme Court upheld in *EPA* v. *EME Homer City Generation, LP.,* 572 U.S. 489 (2014)). In *Coalition for Responsible Regulation* v. *EPA (CRR),* the Court considered a challenge to the EPA's 2009 determination under CAA section 202(a) that GHG air pollution may reasonably be anticipated to endanger public health and welfare (the GHG Endangerment Finding) on grounds that the EPA had failed to quantify a threshold amount of GHG air pollution that would be safe and that, as a result, the EPA had no basis for concluding that the current amount may endanger. 684 F.3d 102, 122–23 (DC Cir. 2012), *aff'd in part and rev'd in part on other grounds sub nom. Utility Air Regulatory Group* v. *EPA,* 573 U.S. 302 (2014). The Court upheld the GHG Endangerment Finding, concluding that the EPA based it on an overall assessment of risk—accounting for ''the precautionary thrust of the CAA and the multivariate and sometimes uncertain nature of climate science''—for which no quantitative threshold is necessary. *Id.* at 123. That case is distinguishable because it focused on the endangerment finding for GHG air pollution, not on the amount of contribution that GHG emissions make to that air pollution. In any event, the contribution requirement of section 202(a)(1) requires only a simple contribution determination, not a significant contribution.

[49] In the EGU CO_2 NSPS Rule, the EPA determined, in the alternative, that CO_2 emissions from fossil fuel-fired EGUs contribute significantly to dangerous air pollution. The EPA explained that fossil fuel-fired EGUs ''emit almost one-third of all U.S. GHG emissions, and are responsible for almost three times as much as the emissions from the next ten stationary source categories combined.'' The EPA added that ''[t]he CO_2 emissions from even a single new coal-fired power plant may amount to millions of tons each year,'' and that ''the CO_2 emissions from even a single NGCC unit may amount to one million or more tons per year.'' The EPA also asserted that in that rulemaking, ''[i]t is not necessary'' for the EPA ''to decide whether it must identify a specific threshold for the amount of emissions from a source category that constitutes a significant contribution.'' The EPA explained that ''under any reasonable threshold or definition, the emissions from combustion turbines and steam generators are a significant contribution.'' 80 FR 64531. In 2018, the EPA proposed to revise the EGU CO_2 NSPS Rule, and solicited comment on whether a SCF for GHG emissions from fossil fuel-fired EGUs was a necessary predicate for promulgating a NSPS for those emissions. ''Review of Standards of Performance for Greenhouse Gas Emissions From New, Modified, and Reconstructed Stationary Sources: Electric Utility Generating Units—Proposed Rule, 83 FR 65424, 65432 n.25 (December 20, 2018). While the EPA has not taken final action

Continued

rulemaking shortly to identify thresholds and/or criteria and to apply them in future significance determinations.

Commenters objected that the 2016 Rule's SCF should not be considered invalid due to the lack of a standard by which to assess significant contribution, citing *Mississippi Commission on Envtl. Quality* v. *EPA,* 790 F.3d 138 (D.C. Cir. 2015) (*Mississippi*), the most recent decision in the line of cases that includes *Catawba,* noted above. In that line of cases, the Court upheld the EPA's approach to determining whether, under CAA section 107(d)(1)(A)(i), an upwind area should be treated as nonattainment because it ''contributes'' to downwind air quality problems. *See Mississippi,* 790 F.3d at 150 (citing *Catawba,* 571 F.3d at 39–40). The Court held that the EPA was not required to establish a threshold level of impact for determining whether an upwind area ''contributes'' to a downwind area. The *Mississippi* Court cited *Catawba,* 571 F.3d at 39–40), which commenters, in turn, cite to argue that such a threshold is not necessary for determining a significant contribution under CAA section 111(b). However, as noted above, the EPA had ''define[d] and explain[ed]'' a set of criteria for determining whether an upwind area ''contributes,'' and in the cited case law, the Court found that these criteria facilitated the reasonableness of the EPA's decision-making. *Catawba,* 571 F.3d at 39–40. In any event, this case law is distinguishable because it concerns the EPA's determination under CAA section 107(d)(1)(A)(i) of a simple contribution, whereas CAA section 111(b) requires the EPA to determine a *significant* contribution. As noted above, the EPA considers it particularly important to develop a set of criteria and/or a standard in order to determine when a significant contribution occurs, in order to distinguish it from a simple contribution.

C. Criteria for Making a Significant Contribution Finding Under CAA Section 111

In the 2019 Proposal, the EPA solicited comment regarding criteria for the Agency to consider in making a SCF. 84 FR 50267. The solicitation for comment was not on the factors the Agency should consider in determining whether air pollution may reasonably be anticipated to endanger public health or welfare, but rather the factors that should be considered when determining under CAA section 111 whether a pollutant from a source category significantly contributes to that air pollution. Several commenters recommend that the EPA defer any action on SCF criteria and suggest the EPA undertake these questions in a separate future rulemaking. Some commenters suggest specific criteria the EPA could consider.

The EPA made clear in the 2019 Proposal that it would not finalize criteria in this rulemaking, but rather would conduct a separate rulemaking to do so. 84 FR 50267. There is no need for the EPA to promulgate criteria at this time because this rule rescinds NSPS. The EPA expects that in the future, it will promulgate criteria before promulgating additional NSPS.

It should be noted that several commenters contend that oil and gas methane emissions are too small to be considered ''significant.'' For example, some commenters cite as support that the contribution of oil and gas methane to total U.S. GHG emissions is only about 3 percent, that U.S. methane emissions are only about 7 percent of global methane emissions, and that U.S. methane emissions are only about 1 percent of global GHG emissions. The EPA appreciates the commenters' views concerning the amounts and impacts of methane emissions from the transmission and storage segment, as well as the production and processing segments. The EPA acknowledges that depending on the criteria that it adopts to support a SCF in the future, such a relatively small contribution to the national and global pool of methane emissions may not be deemed significant. But until the EPA itself reviews and assesses those amounts of emissions according to the criteria that it eventually adopts, the EPA cannot make a determination as to whether methane emissions from the production and processing segments contribute significantly to dangerous air pollution.

VII. Implications for Regulation of Existing Sources

As discussed in section VII of the proposal preamble, the EPA recognizes that by rescinding the applicability of the NSPS, issued under CAA section 111(b), to methane emissions for the sources in the Crude Oil and Natural Gas Production source category that are currently covered by the NSPS, existing sources of the same type in the source category will not be subject to regulation under CAA section 111(d). This is a legal consequence that results from the application of the CAA section 111 requirements. Comments were received that both agreed and disagreed with the proposed decision and reflected varying opinions on the implications for regulation of existing sources. These comments are provided, along with the EPA's responses, in section X of this preamble and in Chapter 9 of the Response to Comments Document. None of the comments received resulted in a material change in the EPA's rationale and conclusions from proposal. The following provides a summary of the EPA's legal interpretation of CAA section 111(d)(1) and rationale for why the lack of regulation of existing sources under CAA section 111(d) will have a limited environmental impact.

A. Existing Source Regulation Under CAA Section 111(d)

As the EPA stated at proposal (see section VII of the 2019 Proposal preamble), CAA section 111(d) authorizes the regulation of existing sources in a source category for particular air pollutants to which a standard of performance would apply if those existing sources were new sources. By legal operation of the terms of CAA section 111(d), certain existing sources in the Crude Oil and Natural Gas Production source category will no longer be subject to regulation under CAA section 111(d) as a result of this final rule. Under CAA section 111(d)(1)(A), CAA section 111(d) applies only to air pollutants (1) for which air quality criteria have not been issued, and which are not on the EPA's list of air pollutants issued under CAA section 108(a) (commonly referred to as the ''CAA 108(a) exclusion''), and (2) which are not HAP emitted from a source category regulated under CAA section 112 (commonly referred to as the ''CAA 112 exclusion''). *See* 42 U.S.C. 7411(d)(1)(A) (CAA section 111(d) applies to ''any air pollutant (i) for which air quality criteria have not been issued or which is not included on a list published under section 7408(a) of this title or emitted from a source category which is regulated under section 7412 of this title'').

For reasons set out in the proposal preamble, the EPA has concluded that VOC fall within the CAA 108(a) exclusion and, thus, are not the type of air pollutant that, if subjected to a standard of performance for new sources, would trigger the application of CAA section 111(d). VOC are not expressly listed as CAA section 108(a) pollutants, but they are precursors to photochemical oxidants (*e.g.,* ozone) and PM, both of which are listed CAA section 108(a) pollutants. As provided in CAA section 302(g), the term ''air pollutant'' is defined to include

for that rule, the unique CO_2 emissions profile of fossil fuel-fired EGUs should be noted: The volume of emissions from EGUs dwarfs the amount of GHG emissions from every other source category.

precursors ''to the extent that the Administrator has identified such precursor or precursors for the particular purpose for which the term 'air pollutant' is used.'' For the following reasons, it is appropriate to consider VOC within the scope of photochemical oxidants and PM, which are listed CAA section 108(a) pollutants, for the particular purpose of applying the CAA section 108 exclusion in CAA section 111(d).

First, VOC are regulated through the CAA's NAAQS implementation program established under CAA section 110, as a result of the inclusion of ozone and PM on the CAA section 108(a) list, because VOC are precursors to those two listed pollutants. See, *e.g.,* CAA section 182(b)(2) (establishing ''reasonably available control technology'' requirements for VOC sources in moderate ozone attainment areas); CAA section 182(c)(2)(b) (requiring serious ozone areas to submit a reasonable further progress demonstration that will account for a set amount of VOC emissions reductions); CAA section 182(d)(2) (requiring specific VOC reductions to satisfy the offset requirement for severe areas); CAA section 182(e)(1) (requiring specific VOC reductions to satisfy the offset requirement for extreme areas). Indeed, the regulation of ozone precursors is the means of addressing ozone in the ambient air, because ozone levels in the ambient air are the result of photochemical reactions of precursors (VOC and NO_X), as opposed to being directly emitted from sources.

Second, as explained in the proposal preamble, excluding VOC from regulation under CAA section 111(d) makes sense within the CAA's three-part structure for addressing emissions from stationary sources. As the EPA has discussed in past rulemakings, the CAA sets out a comprehensive scheme for air pollution control, addressing three general categories of pollutants emitted from stationary sources: (1) Criteria pollutants (which are addressed in CAA sections 108 through 110); (2) hazardous pollutants (which are addressed under CAA section 112); and (3) ''pollutants that are (or may be) harmful to public health or welfare but are not or cannot be controlled under [CAA] sections 108–110 or 112.'' ''Carbon Pollution Emission Guidelines for Existing Stationary Sources: Electric Utility Generating Units: Final Rule,'' 80 FR 64661, 64711 (October 23, 2015) (quoting 40 FR 53340 (November 17, 1975)). Within this three-part structure, CAA section 111(d) is properly understood as a ''gap-filling'' measure to address pollutants that are not addressed under either the criteria pollutant and NAAQS implementation provisions in CAA sections 108 through 110 or the HAP provisions in CAA section 112. Because VOC are regulated as precursors to ozone and $PM_{2.5}$ under CAA sections 108 through 110, they are properly excluded from regulation under CAA section 111(d) because the ''gap-filling'' function of CAA section 111(d) is not needed.

Third, reading the phrase ''included on a list published under [CAA section 108(a)]'' as including precursors is reasonable in light of the provision in CAA section 112(b)(2) that restricts what pollutants may be listed as CAA section 112 HAP.

Finally, as discussed in detail in the proposal preamble, the fact that precursors are not always treated as CAA section 108(a) listed pollutants under all contexts across the CAA does not undermine the conclusion that they should be excluded under the CAA section 108 exclusion in CAA section 111(d).

B. Impact of Lack of Regulation of Existing Oil and Natural Gas Sources Under CAA Section 111(d)

The EPA maintains its position from the proposed rule that the lack of regulation of existing sources under CAA section 111(d) through an Emission Guideline (EG) will have limited impact. This is because there are several factors that will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources even in the absence of an EG.

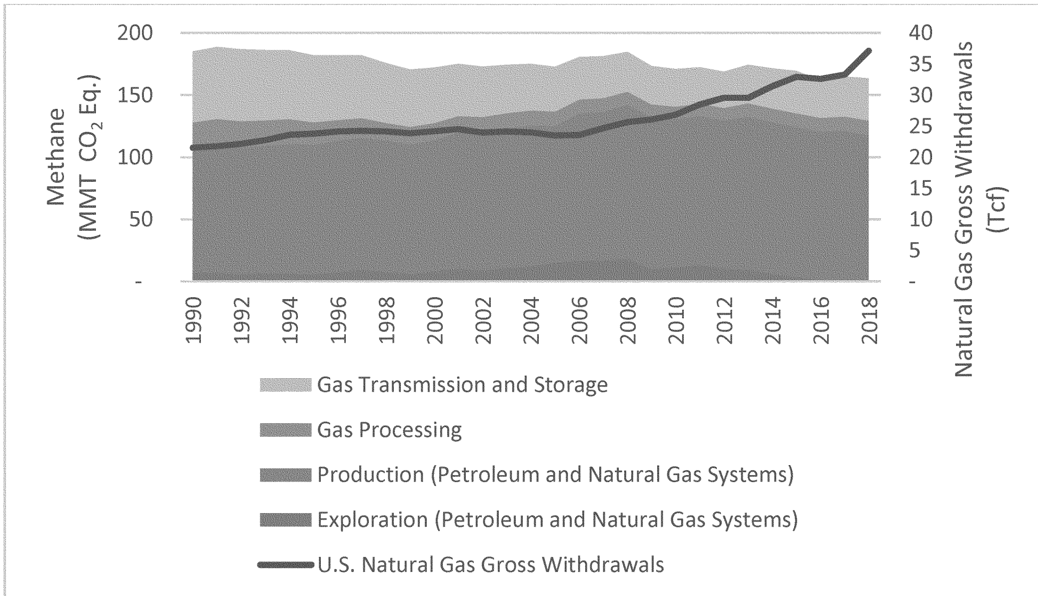
First, as the EPA stated in the 2019 Proposal preamble, the 2016 Rule includes a definition and approach to determining new source applicability that are very broad, and in the specific context of the oil and natural gas production industry, can be anticipated to result in wide applicability of the NSPS to existing sources due to the frequency with which such sources can be reasonably expected to engage in ''modification'' activity. Specifically, it would take at least 7 years from date of promulgation of an EG for requirements to be fully implemented.[50] During this time, the EPA expects that a percentage of existing sources will shut down or undertake modification which will result in them becoming subject to regulation under CAA section 111(b). However, based on limited information that commenters submitted, the EPA acknowledges there may be some existing sources that have never been modified and accepts that these are examples of existing sources that have continued to operate for long periods of time without being reconstructed or modified. The EPA did not prepare and include a quantitative analysis that estimates the levels at which source modification/equipment turnover may occur. However, the EPA maintains that this is one factor (among other factors) that in the absence of an EG will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources.

Secondly, there are market incentives for the oil and natural gas industry to capture as much natural gas (and, by extension, methane) as is cost effective. Depending on the future trajectories of natural gas prices and the costs of natural gas capture and emission reductions, market incentives may continue to drive emission reductions, even in the absence of specific regulatory requirements applicable to methane emissions from existing sources. Assessing the relationship of methane emissions and natural gas production, overall natural gas gross withdrawals have increased about 50 percent from 1990 to 2018, while aggregate methane emissions from the NSPS subpart OOOOa-relevant industry segments have stayed relatively flat (Figure 1). This trend indicates decreasing aggregate methane emissions intensity for these segments over this period (Figure 1). These trends are likely driven by a combination of economic and technical advances.

[50] This estimation considers the development of states' plans and the Federal plan. Unlike NSPS, EG are not directly enforceable; thus, these mechanisms are critical for implementation.

[51] Methane emissions from Table 3–37 (Petroleum Systems) and Table 3–57 (Natural Gas Systems) in U.S. EPA. 2020. Inventory of U.S. Greenhouse Gas Emissions and Sinks: 1990–2018. EPA 430–R–20–002. Available at: *https://www.epa.gov/ghgemissions/inventory-us-greenhouse-gas-emissions-and-sinks-1990-2018.* Accessed July 1, 2020. U.S. Energy Information Administration (EIA) data on natural gas gross withdrawals available at: *https://www.eia.gov/dnav/ng/ng_prod_sum_a_EPG0_FGW_mmcf_a.htm.* Accessed July 1, 2020.

FIGURE 1. NET EMISSIONS OF METHANE EMISSIONS (FROM 2020 GHGI) and U.S. NATURAL GAS GROSS WITHDRAWALS IN TRILLION CUBIC FEET (TCF) (FROM U.S. ENERGY INFORMATION ADMISTRATION NATURAL GAS DATA), 1990 TO 2018.[51]



While environmental performance is a challenging concept to quantify in monetary terms, improving such performance is increasingly important for firms that seek to maintain a ''social license to operate.'' Generally speaking, the social license to operate means that the firm's employees, investors, customers, and the general public find that the firm's business activities and operations are acceptable to continue to freely participate in the marketplace. Maintaining the social license by improving environmental performance, such as reducing emissions, can help firms respond to the complex environment within which they operate in ways that are favorable to their longer-term business interests.

Third, the EPA maintains, and has received a substantial amount of comments confirming its position that participation in the various voluntary methane emissions mitigation programs is one factor (among other factors) that in the absence of an EG that will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources. Owners and operators of facilities in the oil and natural gas industry participate in voluntary programs that reduce their methane emissions. Specifically, many owners and operators of facilities participate in two EPA partnership programs: The Natural Gas STAR Program[52] and the Methane Challenge Program.[53] Owners and operators also participate in voluntary programs that are not administered by the EPA, such as the Environmental Partnership[54] and the Climate and Clean Air Coalition (CCAC) Oil & Gas Methane Partnership.[55] Firms might participate in voluntary environmental programs for a variety of reasons, including attracting customers, employees, and investors who value more environmentally responsible goods and services; finding approaches to improve efficiency and reduce costs; and reducing pressures for potential new regulations or helping shape future regulations.[56][57] The EPA does acknowledge that the industry as a whole is not uniformly meeting voluntary measures at the same level of control and that some companies may not be participating in cited voluntary methane emissions programs at all. This makes it difficult to verify the impacts on emissions as a result of voluntary program participation. Additional time will be needed to allow these programs to further develop and to be fully implemented to better quantify the impacts the varied programs have on

[52] The Natural Gas STAR Program started in 1993 and seeks to achieve methane emission reductions through cost-effective best practices and technologies. Partner companies document their voluntary emission reduction activities and report their accomplishments to the EPA annually. Natural Gas STAR includes over 100 partners across the natural gas value chain and has eliminated nearly 1.39 trillion cubic feet of methane emissions since 1993.

[53] The Methane Challenge Program, started in 2016 and designed for companies that want to adopt more ambitious actions for methane reductions, expands the Natural Gas STAR Program through specific, ambitious commitments; transparent reporting; and company-level recognition of commitments and progress. This program includes more than 50 companies from production, gathering and boosting, transmission and storage, and distribution.

[54] The Environmental Partnership is composed of various companies of different sizes and includes commitments to replace all high-bleed pneumatic controllers with low-bleed controllers (*i.e.,* controllers with a bleed rate less than 6 scfh) within 5 years, require operators to be on-site or nearby when conducting liquids unloading, and require initial monitoring for fugitive emissions at all sites within 5 years, with repairs completed within 60 days of fugitive emissions detection. *https://theenvironmentalpartnership.org/.*

[55] The CCAC Oil and Gas Methane Partnership is a technical partnership between oil and natural gas companies, the Environmental Defense Fund, the EPA Natural Gas STAR Program, and the Global Methane Initiative that provides technical documents on a wide variety of opportunities for reducing methane emissions and requires annual progress reports from its participants. Yearly data on the progress being made by participants is available on the CCAC website. *http://ccacoalition.org/en/content/oil-and-gas-methane-partnership-reporting.*

[56] Borck, J.C. and C. Coglianese (2009). ''Voluntary Environmental Programs: Assessing Their Effectiveness.'' Annual Review of Environment and Resources. 34(1): 305–324.

[57] Brouhle, K., C. Griffiths, and A. Wolverton (2009). ''Evaluating the role of EPA policy levers: An examination of a voluntary program and regulatory threat in the metal-finishing industry.'' Journal of Environmental Economics and Management. 57(2): 166–181.

reducing emissions from oil and natural gas industry sources.

Fourth, several major oil and natural gas producing states have established regulations on oil and natural gas sector emissions. The EPA recognizes that state requirements vary in stringency and that only a subset of states include requirements for sources that the EPA could potentially define as existing sources. However, states that have standards applicable to existing sources include California, Colorado, Utah, Wyoming (in the Upper Green River Basin ozone non-attainment area), and Texas, and account for a substantial portion of oil [58] and natural gas production [59] in the United States. Furthermore, current state regulations (and permits) controlling VOC emissions will concurrently reduce methane emissions from the oil and natural gas industry. For example, areas that are designated Moderate nonattainment and above for certain ozone NAAQS, and states within the Ozone Transport Region, are required to adopt and implement VOC controls for oil and gas sources covered by the EPA's 2016 Control Techniques Guidelines.[60] These controls, which the EPA will address through the state implementation plan (SIP) approval process, will concurrently reduce methane emissions.

As with other factors cited by the EPA, existing source state requirements are one factor (among others) that in absence of an EG will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources. Further detail regarding comments received on the potential for limiting emissions from existing sources can be found in section X of this preamble.

VIII. Summary of Major Comments and Responses

In this section, we respond to many of the major comments made on the 2019 Proposal. In the Response to Comments Document in the docket, we provide additional discussion for some of these comments, and respond to additional comments.

A. Revision of the Source Category To Remove Transmission and Storage Segment

1. History of Scope of Oil and Natural Gas Source Category

Comment: Commenters assert that language in CAA section 111 demonstrates that Congress contemplated that source categories would be broad and encompass a variety of different types of emission sources. The commenters disagree that the 1979 listing did not include the natural gas transmission and storage segment, and add that, in 1980, the Agency explained: ''Source categories are intended to be broad enough in scope to include all processes associated with the particular industry.'' Commenters state that, in practice, the EPA has long listed broad source categories, covering an entire industry or a source that may be found in numerous industries, and sometimes establishing different subcategories within source categories, including electric utilities, non-metallic mineral processing, and compressor engines. The commenters contend that the EPA's treatment of other source categories soon after the priority listing process consistently recognized the interrelatedness of facilities or of emissions controls for those facilities and that this helps determine what sources to include in each source category. Although petroleum refineries are a separate source category under CAA section 111, the commenters note that the EPA previously explained that the source category for the asphalt roofing industry ''encompasses not only asphalt roofing plants but certain production units at oil refineries and asphalt processing plants which were not included on the Priority List promulgated on August 21, 1979.'' 45 FR 76405.

Response: The EPA has generally exercised discretion in identifying the scope of any particular industry, including which industrial processes it includes, for purposes of treating it as a source category under CAA section 111.[61] The EPA acknowledges that some of the listed source categories were broad in scope. However, the EPA has also listed source categories that are relatively narrow in scope—they have distinct facility boundaries that encompass a particular process that, in turn, follows a linear path and results in a specific product. Examples of narrowly defined source categories include the following.

- *Primary Copper Smelting, Subpart P:* A primary copper smelter is any installation or any intermediate process engaged in the production of copper from copper sulfide ore concentrates through the use of pyrometallurgical techniques. The affected facilities in primary copper smelters are dryers, roasters, smelting furnaces, and copper converters.
- *Nitric Acid Plants, Subpart G and Ga:* A nitric acid plant is a nitric acid production unit, which, in turn, is any facility producing weak nitric acid by either the pressure or atmospheric pressure process.
- *Kraft Pulp Mills, Subparts BB and BBa:* A kraft pulp mill is any stationary source which produces pulp from wood by cooking (digesting) wood chips in a water solution of sodium hydroxide and sodium sulfide (white liquor) at high temperature and pressure. Regeneration of the cooking chemicals through a recovery process is also considered part of the kraft pulp mill. The affected sources are digester systems, brown stock washer systems, evaporator systems, condensate stripper systems, recovery furnaces, smelt dissolving tanks, and lime kilns at kraft pulp mills.
- *Sulfuric Acid Plants, Subpart H:* The affected sources are sulfuric acid production units. These are defined as any facility producing sulfuric acid by the contact process by burning elemental sulfur, alkylation acid, hydrogen sulfide, organic sulfide and mercaptans, or acid sludge, but do not include facilities where conversion to sulfuric acid is utilized primarily as a means of preventing emissions to the atmosphere of sulfur dioxide or other sulfur compounds.

If the EPA does not originally include in a listing certain processes, and subsequently seeks to include those processes, the EPA must make the requisite statutory findings in order to do so. The action that the commenters cite supports this point. In the original 1979 Priority List, the EPA listed the Asphalt Roofing Plants source category. Subsequently, based on studies on the asphalt roofing industries, the EPA determined that the initial processing of asphalt for roofing manufacture may take place at sources other than asphalt roofing plants. Accordingly, the EPA, through rulemaking, amended the 1979 source category listing to include additional locations such as asphalt processing plants and asphalt storage tanks at oil refineries. *See* 45 FR 76427 and 28. In doing so, the EPA provided a specific rationale for broadening the source category. The present situation

[58] Approximately 52 percent of crude oil production in 2019 according to *https://www.eia.gov/dnav/pet/pet_crd_crpdn_adc_mbblpd_a.htm.*

[59] Approximately 35 percent of natural gas production in 2019 according to *https://www.eia.gov/dnav/ng/ng_prod_sum_a_EPG0_VGM_mmcf_a.htm.*

[60] On October 27, 2016, the EPA provided notice of the availability of a final control techniques guideline document titled *Control Techniques Guidelines for the Oil and Natural Gas Industry* (EPA 453/B–16–001). 81 FR 74798 (October 27, 2016).

[61] The EPA has not relied on particular formulations, such as standard industrial classification, to identify an industry for purposes of classifying it.

requires a similar analytical framework: (1) The original source category listing for Crude Oil and Natural Gas Production was not broadly defined to include transmission and storage, and (2) the requisite statutory findings have not been made to expand the category to include it.

Comment: Several commenters assert that nothing in the 1979 listing decision supports the EPA's claim that the Agency at the time viewed facilities used in natural gas transmission and storage (*e.g.,* stationary pipeline compressor engines) as a separate source category.

Another commenter asserts that the omission in the 1979 listing of a source in the transmission and storage segment that had been included in the 1978 technical document suggests that this source was incorporated into the Crude Oil and Natural Gas Production source category. The commenter states that, while the EPA studied Stationary Pipeline Compressor Engines, which are found in the transmission and storage segment, as a potential independent source category in the 1978 technical document,[62] this source was not listed as a major or minor source in the 1979 Listing.[63] The commenter states that, while the Agency argues that the source was included in the Stationary Internal Combustion Engines listing, the EPA supports this proposition only by citing to a 2008 rule, which does not expressly include stationary pipeline compressor engines within the Stationary Internal Combustion Engines source category.[64] The commenter notes that the EPA cites to a page stating that ''[c]ategories and entities potentially regulated by this action'' include ''[a]ny manufacturer that produces or any industry using a stationary internal combustion engine as defined in the final rule.'' 73 FR 3568 and 69. The preamble contains a list of ''[e]xamples of regulated entities'' that includes ''[n]atural gas transmission.'' 73 FR 3569. However, according to the commenter, the applicability criteria of the final rule contains no explicit reference to stationary pipeline compressor engines.

Response: As a general matter, the Agency has the authority to revisit its prior categorization determinations. Nonetheless, the EPA, upon a close read of its prior rules believes that this and certain other comments on prior Agency determinations are mistaken, as described further in this section. The EPA notes that while it believes the 1979 listing did not include the transmission and storage segment for the reasons described in this final rule, any interpretation otherwise (*i.e.,* that the listing did include this segment) did not have any practical effect until the 2012 Rule, when the EPA promulgated standards for this segment for the first time. Therefore, to the extent the 1979 listing can be considered to have included the transmission and storage segment, the EPA is alternatively determining that such inclusion was incorrect for the same reasons why the 2012 and 2016 Rules incorrectly included the segment as part of the source category.

The EPA disagrees with the commenter's suggestion that the 1979 listing incorporated stationary pipeline compressor engines into the Crude Oil and Natural Gas Production source category. This is clearly evidenced by examining the pollutants which are identified for the category. For the 1979 listing, the pollutants identified for the Crude Oil and Natural Gas Production source category were VOC and SO_2. In the 1978 background documentation, the pollutants identified for stationary pipeline compressor engines were NO_X, SO_2, and carbon monoxide (CO). If the EPA had included stationary pipeline compressor engines in the Crude Oil and Natural Gas Production source category in 1979, the Agency likely would have added NO_X and CO to the list of pollutants for the category.

That the Stationary Internal Combustion Engine rule (40 CFR part 60, subpart IIII) covers engines in the natural gas transmission and storage segment is further evidenced by the statement from the February 26, 2008, **Federal Register** document that specifically identifies engines in natural gas transmission as example entities subject to the rule. The commenter is incorrect in asserting that the applicability criteria of the regulations are silent on engines in natural gas transmission. Those applicability criteria are *characteristics* of the engine (*e.g.,* maximum engine power), which are unrelated to the *location* of the engine (*e.g.,* in the transmission segment). *See* § 60.4230 of 40 CFR part 60, subpart JJJJ. Therefore, the lack of explicit mention of the transmission segment does not mean that engines in that segment are not included in the category.

Comment: Several commenters stated that the description of the Crude Oil and Natural Gas Production source category in the 1984 proposed NSPS for VOC and SO_2 emissions made clear that the category did not include transmission and storage operations. The commenters pointed to the statement in the preamble that the source category excluded emission sources related to the ''distribution'' of products ''to petroleum refineries and gas pipelines'' (citing, *e.g.,* 49 FR 2636.

Other commenters disagree. One commenter asserts that the EPA defined the source category as ''encompass[ing] the operations of exploring for oil and natural gas products, drilling for these products, removing them from beneath the earth's surface, and processing these products from oil and gas fields for distribution to petroleum refineries and gas pipelines.'' The commenter states that it is clear that compressor stations within the transmission and storage segment ''process these products . . . for distribution'' by compressing the gas and forcing it through the pipelines.

Response: The EPA does not agree with the commenter's interpretation of the quotation from the 1984 proposal. Specifically, the EPA does not agree that the compression of the natural gas along transmission pipelines constitutes processing of the natural gas. Natural gas processing has historically been defined by the Agency to include the extraction of natural gas liquids from field gas, fractionation of mixed natural gas liquids to natural gas products, or both. (40 CFR part 60, subpart KKK; 40 CFR part 63, subpart HH). The EPA maintains that the language in the 1984 proposal, *i.e.,* that the category includes ''the operations of exploring for oil and natural gas products, drilling for these products, removing them from beneath the earth's surface, and processing these products from oil and gas fields for distribution to petroleum refineries and gas pipelines,'' is not ambiguous. Following the well-defined ''processing'' operations, the natural gas enters transmission gas pipelines. These are the gas pipelines referred to in the 1984 preamble, meaning that the gas leaves the processing segment of the oil and natural gas production source category and travels to the next segment, the natural gas transmission pipelines.

Comment: One commenter asserts that, within the 1984 definition of the production segment, the EPA drew a definitional boundary whereby production consisted of extraction ''and processing [of oil and natural gas] for distribution to petroleum refineries and gas pipelines.'' The commenter states that this implies that the boundary at which the Agency has always historically defined the category as being where production meets local distribution to pipelines or refineries. The commenter states that this interpretation of the CAA meant that the

[62] U.S. EPA. Priorities for New Source Performance Standards Under the Clean Air Act Amendments of 1977. April 1978. EPA–450/3–78–019. p. 33.

[63] 44 FR 49222 through 49226.

[64] 73 FR 3568, 3569 (January 18, 2008).

production segment abuts the distribution end of the industry—not an arbitrarily created ''Transmission and Storage'' segment.

Response: The EPA's use of the term ''distribution'' in the 1984 preamble was misinterpreted by the commenter. The commenter appears to interpret ''distribution'' as the distribution segment of the natural gas industry, and that the source category includes everything up to that segment. In the context of the 1984 preamble, the EPA's use of the term ''distribute'' means the transfer to the next segment of the industry.

Comment: A commenter asserts that the 1984 proposal serves to demonstrate that the EPA did not view its listing as constrained to its literal terms—''Crude Oil and Natural Gas Production''—because the 1985 NSPS regulated the processing, not the production, segment of the natural gas industry. Specifically, the EPA stated that, with regard to the discussion of equipment leaks, ''equipment used in crude oil and natural gas production (not to be confused with natural gas processing) for equipment leaks of VOC is not appropriate for widely dispersed equipment.'' 49 FR 2637. The commenter states that, taken to a literal extreme, the proposal's argument would mean that the 1985 NSPS exceeded the scope of the source category and was, thus, unlawful.

Response: The EPA agrees that the language that the commenter quotes indicates the Agency's view in the 1985 NSPS that the source category covered both production and processing. However, this does not in turn mean that the Agency thought that the source category included the transmission and storage segment as well. As described above, the 1984 proposal acknowledged equipment leaks in the production segment but declined to set standards for them based on a technical analysis. This discussion makes clear that the Agency considered production to be part of the source category. In contrast, as discussed above, the preamble is silent on equipment leaks in the transmission and storage segment.

Comment: Further, the commenter states that the EPA's proposal appears to concede that the Agency has never been limited to regulating only those specific sources within the listed category that it regulated in the first NSPS. The commenter states that, prior to 2012, the EPA had issued standards for emissions at gas processing plants only as part of the ''Crude Oil and Natural Gas Production.'' The commenter notes that in 2012 the EPA regulated VOC from previously unregulated upstream sources, including well completions, centrifugal compressors, reciprocating compressors, pneumatic controllers and storage vessels (citing 77 FR 49490 (Final Rule promulgating 40 CFR part 60, subpart OOOO)). The commenter states that these sources were not part of the EPA's analysis in 1979 or 1984 NSPS, yet the proposal does not suggest that they were improperly regulated in the 2012 Rule. Specifically, in 2012 the EPA stated: ''[i]n addition to the operations covered by the existing standards, the newly established standards will regulate volatile organic compounds from gas wells, centrifugal compressors, reciprocating compressors, pneumatic controllers and storage vessels'' (citing 77 FR 49490).

The commenter also indicates that the EPA's citation to the 1984 NSPS ignores other statements made during other rulemakings for the source category, including the same 1984 rulemaking, that suggest that the source category was intended to cover broadly the oil and natural gas sector, or at least was not limited to production and processing (citing 84 FR 50256). The commenter states that, in that NSPS, the EPA felt the need to exclude specifically certain sources found in the transmission and storage segment from the standards it set, something that would not have been necessary if the Agency had intended to exclude these segments themselves from the definition of the source category. The sources excluded in that NSPS are compressor stations, dehydration units, sweetening units, underground storage facilities, and field gas gathering systems, unless the facility is located at an onshore natural gas processing plant.

Response: The commenter's representation of the 1984 rulemaking is not entirely accurate. It is true that the 1984 proposal limits the sources covered to those at natural gas processing facilities. However, the EPA does not agree that this rulemaking was an expansion of the original ''Crude Oil and Natural Gas Production'' source category. The commenter is implying that natural gas processing operations were not included in the original source category listing in 1979 but does not provide any evidence from the 1978/1979 actions to support that assertion. An alternative interpretation of this text could also be that the Agency wished to make it sufficiently clear that while sources in part of the production and processing segment are included in the source category, the same sources that are part of the transmission and storage segment are not included in the source category. However, in the absence of an explanation for this exclusion, the most that can be taken away from this text is that these sources are not subject to the 1984 NSPS; this text alone is not dispositive on whether these sources are included in the broader Oil and Natural Gas source category. Therefore, the commenter extrapolates a conclusion without a basis to do so. The fact that SO_2 was a pollutant identified for the Crude Oil and Natural Gas Production source category clearly shows that processing was included, as the sweetening units covered by the 1984 proposed rules are the primary source of SO_2 emissions in the oil and natural gas industry.

In addition, there are numerous statements made by the EPA throughout the 1984 proposal that clearly demonstrate consideration of sources across the entire Crude Oil and Natural Gas Production source category. The commenter cites the statement in the1984 proposal that emission points can be divided into three categories and uses this statement to argue that the source category included transmission and storage. However, the comment fails to include the remainder of the paragraph that includes that statement:

> These emission points can be divided into three main categories: Process, storage, and equipment leaks. Process emission sources include well systems, field oil and gas separators, wash tanks, steeling tanks, and other sources. *These process sources remove the crude oil and natural gas from beneath the earth and separate gas and water from the crude oil. Best demonstrated control technology has not been identified for these process emission points; therefore, these sources have not been considered in developing the proposed standards.* 49 FR 2637 (emphasis added).

This part of the paragraph clarifies two points. First, the EPA clearly considered the upstream sources (well systems, field oil and natural gas separators, etc.) as part of the source category but indicated that since best demonstrated control technology had not been identified for those sources, no standards were being proposed at that time. These sources were then addressed in the 2012 rulemaking, when the best demonstrated technology/BSER had been determined for them. Second, this discussion did not mention operations in the transmission segment.

One commenter also refers to the parenthetical in the 1984 proposal related to oil and natural gas production and argues that it is proof that natural gas processing was not included in the Crude Oil and Natural Gas Production source category. The following provides more of the discussion to provide the full context.

> Equipment leaks of VOC can occur from pumps, valves, compressors, opened ended

lines or valves, and pressure relief devices used in onshore crude oil and natural gas production. These leaks usually occur due to design or failure of the equipment. Equipment used in crude oil and natural gas production (not to be confused with natural gas processing) are widely dispersed over large areas. The analysis presented in the BID for the principal control technique (leak detection and repair work practices) for equipment leaks of VOC is not appropriate for widely dispersed equipment. The costs and emission reduction numbers for such an analysis are unknown at this time. Thus, the proposed standards do not apply to equipment associated with crude oil and natural gas production. The proposed standards apply only to equipment located at onshore natural gas processing plants. 49 FR 2637.

Taking the 1984 preamble excerpt in context illustrates that the distinction made between production and processing was specifically related to the application of leak detection and repair work practices for equipment leaks and not to define the source category. In fact, the discussion makes it clear that the EPA's definition of the source category includes production and processing. Again, there is no mention here of the application of leak detection and repair programs to the transmission and storage segment.

Finally, the commenter cites a paragraph from the proposed regulation, which clarifies that sources not located at a natural gas processing plant are not affected facilities, as evidence that the category includes the transmission and storage segment, since ''compressor stations'' are included. This is also not a compelling argument. It is not uncommon for equipment, other than that used to extract natural gas liquids from field gas or to fractionate mixed natural gas liquids to natural gas products, to be located at a natural gas processing plant. This paragraph—40 CFR 60.630(e)—simply clarifies that if other operations (*i.e.,* compressor stations, dehydration units, sweetening units, underground storage facilities, field gas gathering units, and liquefied natural gas units) are located at a natural gas processing plant, the associated components are subject to the leak detection and repair requirements in NSPS subpart KKK. This list cannot be extrapolated to the conclusion that the EPA considered all these operations to be in the source category. As evidence of this note that ''liquefied natural gas units'' are included in the list. These units, while part of the overall oil and natural gas industry, have never been contemplated as being part of the Crude Oil and Natural Gas source category.

2. ''Sufficiently Related'' Test and Whether Transmission and Storage Operations Are Distinct From Production and Processing

Comment: Commenters contend that the proposal to amend the source category definition is fundamentally at cross-purposes with the proposal to remove standards of performance for methane. The EPA proposed to justify the latter by finding that regulation of methane and VOC is redundant because the controls that sources are required to implement to reduce their VOC emissions will also reduce their methane emissions, and this is true regardless of the relative amounts of VOC and methane in their overall emissions. The commenters state that if methane regulation is redundant on those grounds, then differences in gas composition cannot be the basis for determining that two distinct source categories are necessary.

Response: The commenters conflate the proposal to remove the transmission and storage segment from the source category with the proposal to rescind the methane requirements for the remaining production and processing segment, without acknowledging that while the substance of each may have technical similarities, each proposal addresses discrete, stepwise legal aspects of CAA section 111(b). Under CAA section 111(b), a source category must first be listed before the EPA can promulgate an NSPS for sources within the category. The EPA proposed the first action of removing the transmission and storage segment from the source category, in part based on the conclusion that the segment was not previously properly added to the source category because there are distinct differences in operations and differences in the emissions profiles between the production and processing segments and the transmission and storage segment. As described further in this section, based on the sufficiently related test, these distinct differences in operations and differences in emissions profile means that the transmission and storage segment requires a separate SCF in order to be properly regulated under CAA section 111(b).

However, once a source category is properly listed and defined, as are the production and processing segments, the inquiry then is what are the appropriate standards of performance for sources within that category. This inquiry is separate from and subsequent to the initial inquiry of whether a source category is properly identified for regulation under CAA section 111(b). For example, the EPA has previously identified sources as appropriately subject to regulation under CAA section 111(b), but then subsequently declined to promulgate standards of performance based on inadequate data. In proposing VOC standards for equipment leaks in oil and gas processing, the EPA declined to apply such standards to equipment in the production segment, which is clearly part of the source category, because it did not have data on costs and emission reduction numbers at that time. 49 FR 2637.

Similarly, here, while the production and processing segments have been properly identified as subject to regulation under CAA section 111(b) through the 1979 listing of the source category, the EPA must then contend with *how* to regulate these segments. Accordingly, the EPA proposed the second action to rescind the methane requirements for the production and processing segments based on the fact that VOC and methane controls are redundant. While the rationales for both actions are premised partly on differences in gas composition, the legal and technical inquiry for each action is different, as these are discrete steps to regulation under CAA section 111(b). Though the findings under each inquiry are similarly premised on differences in gas composition, that does not mean that the response to both inquiries must be the same, as each inquiry is distinctly different from one another (*i.e.,* one is whether the transmission and storage segment is properly part of the source category, the other is whether and how to regulate methane from the production and processing segments). The rationale for this second action was also discussed at length in section IV.D of the 2019 Proposal (84 FR 50259 and 50260). The comments received and the EPA responses on this second action are provided in section VIII.B below.

Comment: Commenters do not agree that the transmission and storage segment cannot be included in the Crude Oil and Natural Gas source category because the gas composition and operations in that segment are too different from those in the production and processing segments. These commenters assert that the EPA's own data do not support the EPA's rationale. The commenters suggest that, while the EPA compares the average composition of the production segment to the average composition of the transmission segment, the Agency fails to consider the extensive overlap in the range of compositions in both segments. The commenters state that the EPA's 2011 Natural Gas Composition memorandum data show the wide range of compositions of gas in the production and transmission segments.[65] The commenters contend that the range of methane compositions in the production segment fully encompasses the range in the transmission segment, demonstrating the similarity of the gas composition in the two segments; similarly, there is extensive overlap between the segments' VOC compositions.

Commenters also discussed the EPA's more recent 2018 composition data,[66] asserting that it shows even more variation in gas composition. A commenter asserts that while the EPA recognizes that variations in the gas composition can occur from basin-to-basin within each segment, the EPA does not acknowledge that these basin-to-basin variations can swamp the purported variations on which the EPA relies to justify a distinction between production and transmission segments.

One commenter states that its experience with the oil and natural gas industry operating in Pennsylvania shows that unprocessed field gas [67] can range from, by volume, 75-percent to 98-percent methane and 0.1-percent to 10-percent VOC. The commenter states that in a number of Pennsylvania counties, the county average field gas composition meets the EPA's pipeline quality gas composition (*i.e.,* is equal to or greater than 93-percent methane and less than or equal to 1-percent VOC; HAP data is unavailable). The commenter states that there are several natural gas well pads that dehydrate the produced gas onsite and transfer custody directly to an interstate pipeline. The commenter notes that this reality further blurs the distinction between the production and the transmission and storage segments. The commenter contends that, if a well site is required to meet the requirements of the 2016 Rule, it stands to reason that a transmission compressor station accepting the same gas should be required to meet the same requirements.

One of the commenters also notes that the 2018 Natural Gas Composition memorandum did not include any updated data for the transmission and storage segment. The commenter states that, given the significant difference in the production segment data from 2011 and 2018, the EPA must collect more current data for the transmission and storage segment if it seeks to justify any claims about the segment being sufficiently distinct from production and processing to warrant revision of the source category.

Response: The EPA recognizes that the composition of natural gas in the production segment can vary considerably, and that in some basins/areas it is possible that the composition can mirror that in the transmission segment. However, while the commenters stress this overlap in the gas composition in limited geographical regions in the U.S., such as in some parts of Pennsylvania, they seem to discount the substantial differences in most areas. For example, for Texas, the EPA's 2011 gas composition analysis showed that the methane content in the production segment was, on average, 80.1 percent, but ranged from 55.0 percent to 97.8 percent.[68] Because the NSPS subpart OOOOa is a nationwide regulation which applies equally across the country, it is most appropriate to consider the average composition for the segments. Further, on a nationwide basis, the data clearly reveal a distinction in the gas composition between the production and processing segments and the transmission and storage segment.

The commenter is correct that the 2018 Natural Gas Composition memorandum did not include data for the transmission and storage segment. The EPA conducted a new analysis which analyzed average methane concentrations using 2015 through 2018 data reported under 40 CFR part 98, subpart W (Petroleum and Natural Gas Systems), of the EPA's GHGRP.[69] This analysis did include recent data for the transmission and storage segment. The EPA found that there is a statistically significant difference between the average methane concentration in natural gas at either the gas production, gathering and boosting, or gas processing [70] industry segments and the average methane concentration in natural gas at either the transmission compression or underground storage segment. This difference further supports the EPA's justification to remove the transmission and storage segment from this source category.

Comment: Several commenters disagree with the EPA's statements in the 2019 Proposal that equipment and operations in the production and processing segments were not interrelated with the transmission and storage facilities. The commenters contend that while the transmission and storage segment serves a different role than the production, processing, and distribution segments, it is still part of the overall oil and natural gas industry and is a necessary element of the source category because it prepares the recovered gas for distribution. They add that, as the 2019 Proposal notes, the processes used to remove impurities (for example, dehydrators) in the production and processing segments are also used in the transmission and storage segment (citing 84 FR 50258). Commenters noted that the 2016 Rule stated that the equipment and operations at production, processing, transmission, and storage facilities are a sequence of functions that are interrelated and necessary for getting the product ready for distribution (citing 81 FR 35838). Commenters also noted that the 2016 Rule also cited the increase in natural gas production from hydraulic fracturing and horizontal drilling as an example of the interrelated nature of the industry—*i.e.,* increased production resulting in an increase in the amount of natural gas needing to be processed and moved to market or stored, which in turn results in increases in emissions across the entire natural gas industry.

Response: The EPA agrees with the commenters that production, processing, transmission and storage are all segments of the oil and natural gas industry and that the transmission and storage segment is a part of the industry because it prepares the recovered gas for distribution.

However, this does not necessitate that all of the segments belong in the same source category for regulatory purposes under CAA section 111. As explained in the 2019 Proposal, the primary purposes of each segment differs. The purposes of the production and processing segments are to explore, drill, extract, and process crude oil and natural gas found beneath the earth's surface. Extracting crude oil and field gas through drilling wells and processing these products for distribution to petroleum refineries and gas pipelines is an industrial process that is distinct from the transmission and storage segment, whose primary purpose is to move to market pipeline quality natural gas through transmission

[65] Memorandum to Bruce Moore, U.S. EPA from Heather Brown, EC/R. ''Composition of Natural Gas for use in the Oil and Natural Gas Sector Rulemaking.'' July 2011. Docket ID Item No. EPA–HQ–OAR–2010–0505–0084.

[66] Memorandum to U.S. EPA from Eastern Research Group. ''Natural Gas Composition.'' November 13, 2018. Docket ID No. EPA–HQ–OAR–2017–0757.

[67] Field gas is described earlier in section V.B of this preamble.

[68] Memorandum to Bruce Moore, U.S. EPA from Heather Brown, EC/R. ''Composition of Natural Gas for use in the Oil and Natural Gas Sector Rulemaking.'' July 2011. Docket ID Item No. EPA–HQ–OAR–2010–0505–0084.

[69] Analysis of Average Methane Concentrations in the Petroleum and Natural Gas Industry Using Data Reported Under 40 CFR part 98 Subpart W. April 6, 2020. Included in Docket ID No. EPA–HQ–OAR–2017–0757.

[70] Methane concentrations at gas processing facilities evaluated in this study are based on the inlet gas composition (as received) by the gas processing facilities.

pipelines by increasing the pressure and to store the gas underground along the pipeline.

The EPA understands that dehydrators are used to remove impurities from the natural gas in both the production and processing segments and in the transmission and storage segment. In the latter segment, dehydrators are occasionally present along transmission pipelines and at natural gas storage facilities to remove water and other impurities that condense as a result of temperature and pressure changes as the gas moves through the pipeline or is stored underground. However, the different uses of dehydrators illustrate the separate functions that the segments have in the industry. In the transmission and storage segment, dehydrators simply remove these impurities as they accumulate in pipelines. In the production and processing segment, dehydrators are a part of the process to change the overall composition of the gas. It is also noteworthy that the EPA included and regulated air toxics emissions from dehydrators in two separate source categories and in two different NESHAP. Dehydrators in the production and processing segments are covered by 40 CFR part 63, subpart HH, and dehydrators in the natural gas transmission and storage segment are covered by 40 CFR part 63, subpart HHH.

The EPA continues to assert that the comparison with the petroleum industry is directly relevant. The commenters insist that the necessary link between the extraction and processing of the natural gas in the production and processing segments and the transmission of the natural gas predetermines that the two segments must be treated as a single source category. However, this same link exists between the extraction and processing of oil, condensate (and other liquids from oil and natural gas wells) in the production segment and the petroleum refineries and pipelines that refine/process and distribute these liquids. However, the commenters do not suggest the interrelatedness of the production and processing sources originally included in the Crude Oil and Natural Gas Production source category with those in the petroleum liquid source categories necessitates that Crude Oil and Natural Gas Production and Petroleum Refineries be combined into one category and regulated together. The EPA applies the same logic to conclude that the fact that the transmission and storage segment is related to the production and processing sources in the Crude Oil and Natural Gas Production source category does not necessarily result in the requirement that they be regulated together. In addition, other instances in which similar source types emitting the same air pollutants and subject to the same types of controls are included in different source categories. For example, leaking pumps, valves, connectors, and other components at a wide variety of types of facilities that emit VOC and GHG are included in different source categories.

3. The Authority To Expand Source Categories and the EPA's Alternative Approach

Comment: One commenter asserts that, while the 2012 Rule and 2016 Rule expanded the source category, this expansion was appropriate considering the statutory mandate that the Administrator should from time to time review the source categories. The commenter states that the purpose of this review was to assure that the EPA periodically consider new scientific developments to ensure that the Agency was continually acting in a way that protected the public health. The commenter adds that the statute provides no guidance regarding the proper scope of a source category, and that Congress left that determination to Agency expertise, so long as the Agency considers the impacts of the source's emissions on public health. According to the commenter, the EPA's expansion of the source category in the 2016 Rule properly considered the source category's impact on the public health. However, the commenter adds, but the EPA's current effort to rescind that expansion is based on alleged procedural errors and fails to consider the public health impacts of the transmission and storage segment. The commenter states that the transmission and storage segment does significantly contribute to the deterioration of public health. The commenter asserts that the natural gas held at storage facilities contains all of the same toxic air pollutants and hazardous chemicals as natural gas does at other stages of the production process, and that the methane and VOC emissions from compressor stations have the same adverse impact on public health regardless of what segment of the source category the methane and VOC emissions are coming from. The commenter suggests that the EPA take this opportunity to do its own analysis to determine whether methane, VOC, and HAP (air toxic) emissions from the transmission and storage segment of the source category adversely impact public health.

Response: The EPA agrees that the CAA authorizes the EPA to review and revise source categories, and that its purpose was to ensure that the Agency was continually acting in a way that protected the public health. However, the EPA disagrees with the commenters' position on the EPA's past consideration of public health in the expansion of the Crude Oil and Natural Gas source category. The EPA's 2015 evaluation of the impacts of GHG, VOC, and SO_2 on public health and welfare (80 FR 56601) was conducted for crude oil and natural gas production and processing, along with natural gas transmission and storage. While it is true, as the commenter points out, that methane and VOC are emitted from the natural gas transmission and storage segment, the EPA's 2015 analysis did not separate the impacts of the pollutants emitted by natural gas transmission and storage to demonstrate that the emissions from this segment contribute significantly to the overall impacts. In the 2019 Proposal, the EPA proposed that it was required to make a finding that the transmission and storage segment, in and of itself, contributes significantly to air pollution which may reasonably be anticipated to endanger public health and welfare. Nothing in the comments provided cause the EPA to change this conclusion.

4. Significant Contribution Finding for Natural Gas Transmission and Storage

Comment: Several commenters state that the SCF that the EPA made in the 2016 Rule, which was for the production, processing, transportation, and storage segments collectively, was not appropriate to authorize the EPA to promulgate NSPS for sources in the transmission and storage segment. The commenters assert that to regulate sources in that segment, the EPA was required to make a SCF determination for emissions from that segment itself. Commenters explain that, to consider otherwise, once the EPA makes a SCF determination for a source category consisting of certain types of sources, the Agency would then be able to add into that source category all manner of ancillary equipment and operations, even if those ancillary equipment and operations do not in and of themselves significantly contribute to the previously-identified endangerment. The commenter states that this would allow the EPA to evade the express listing criteria by lumping loose associations of nominally related segments of an industry into a sector.

Other commenters disagreed, stating that in the 2016 Rule, the EPA determined that the rulemaking record supported a revision of the source category listing to include broadly the entire oil and natural gas industry (*i.e.,* production, processing, transmission and storage) that, in the Administrator's judgment, contributes significantly to air pollution which may reasonably be anticipated to endanger public health or welfare. Commenters add that CAA section 111(b)(1)(A) grants the Administrator authority to ''from time to time . . . revise'' the listed categories, and that nothing in the statutory text or relevant case law suggests that the EPA must, before revising a source category in a way that expands its scope, make a SCF determination for the newly added part of the category, considered alone. The commenter adds that nothing in the statute indicates that Congress intended for it to be more difficult for the EPA to add sources to a category than to include those sources in the category in the first instance. The commenter states that the EPA's obligation when revising a source category is only to conclude that the entire category, as revised, can still be deemed to contribute significantly to pollution that endangers public health or welfare.

Response: In this action, the EPA is determining that the transmission and storage segment of the oil and natural gas industry should not be included with the production and processing segments as a single source category. For that reason, if, in the future, the EPA seeks to promulgate standards of performance for any air pollutants from the transmission and storage segment, it must first list the segment as a source category and then determine that their emissions cause or contribute significantly to air pollution reasonably anticipated to endanger public health or welfare (SCF). Commenters take different positions on the question of whether the EPA must make a SCF for the transmission and storage segment as a predicate to adding them into a source category that already includes the production and processing segments. However, because the EPA is determining that the transmission and storage segment was not properly added to the source category, it is not necessary to resolve that question, and the EPA does not do so in this action.

Comment: Several commenters assert that, in order to remove transmission and storage segment sources from the Oil and Natural Gas source category, the EPA must affirmatively show that emissions from the sources do not significantly impact public health.

Response: The EPA disagrees with this comment. In this action, the EPA is determining that its previous determinations that the Crude Oil and Natural Gas source category included the transmission and storage segment beginning in 1979, or, in the alternative, that the EPA was justified in expanding the category to include that segment, were improper. Rather, the EPA is determining that the source category did not include that segment beginning in 1979 and that the EPA's action in 2012 and 2016 to add this segment into the source category was improper. These reasons justify the EPA in determining that the proper scope of the source category is the production and processing segments alone. There is no requirement under CAA section 111 that the improperly added segment must remain in the source category until the EPA determines that they do not cause or contribute significantly to dangerous air pollution.

5. Whether EPA Must Move To Add/Expand the Source Category and Regulate Transmission and Storage Emission Sources

Comment: Several commenters suggest that if the EPA finalizes the proposal to remove natural gas transmission and storage and rescind the applicable requirements for this segment, that the EPA should also move to properly and legally expand the source category and regulate natural gas transmission and storage emission sources. The commenters state that, beyond asserting that it might do so in the future, the proposal fails to explain why it does not take the logical next step and assess whether the emissions from the transmission and storage segment contribute significantly to dangerous pollution. The commenters contend that the current record, as well as the EPA's past findings, demonstrates that the emissions from the transmission and storage segment by itself does contribute significantly to dangerous air pollution.

Response: The EPA determined that the Agency's past interpretations and actions related to the inclusion of the transmission and storage segment in the Crude Oil and Natural Gas Production source category were in error. This action focuses on the correction of these past errors and interpretations. The EPA posits that retaining this focus, in the absence of established SCF criteria for GHG emissions/methane needed to add/expand the scope of this rulemaking, is necessary and appropriate, and that doing so provides greater clarity and certainty for the regulated community.

The EPA agrees with commenters that if an appropriate assessment of the emissions from the transmission and storage segment concludes that emissions from this segment contribute significantly to the endangerment to public health or welfare, we would need to propose a separate rulemaking for the regulation of emissions from sources in this segment. However, the EPA is not, at this time, assessing whether the emissions from the transmission and storage segment contribute significantly to the endangerment to public health or welfare.

Further, the proposal preamble solicited comment regarding appropriate criteria for the EPA to consider in making a SCF. This request was made both as a broad matter and with particular reference to GHG emissions generally, and to methane emissions from the Oil and Natural Gas source category most particularly. The EPA is evaluating the responses received to its solicitation and has not yet established criteria that it would follow to make such a SCF for the transmission and storage segment as it relates to GHG emissions/methane. Discussion on comments received on the EPA's solicitation related to SCF criteria can be found in section VI.C of this preamble.

B. Rescission of the Applicability to Methane of the NSPS for Production and Processing Segments

The following summarizes some of the major comments on the EPA's proposal to rescind the methane NSPS for the production and processing segments and provides the EPA's responses. Additional discussion and comments and responses on this topic are provided above, in section V.B, and in Chapter 6 of the Response to Comments Document.

Comment: Several commenters do not agree with the proposal that section 111 of the CAA authorizes the EPA to rescind one pollutant's standards because another pollutant's standards may capture them. The EPA claims that it lacked a rational basis for its 2016 action because the requirements added in 2016 are entirely redundant with the existing NSPS for VOC. However, commenters indicate that there is not a specific provision within the CAA that expressly exempts pollutants from regulation due to overlapping control technology.

Response: Although it is true that no CAA provision explicitly authorizes rescinding requirements on the ground that they are redundant, the EPA's basis for this action is that it erred in the 2016 Rule when it concluded that it had a rational basis to regulate methane. It is not rational to impose redundant requirements, because they are not necessary and do not achieve additional health or environmental protections. This basis for the EPA's action does not depend on explicit statutory authorization.

Comment: Multiple commenters support removing methane requirements for the production and processing segments on the ground that they are redundant with the existing NSPS for VOC, for the reasons the EPA stated in the 2019 subparts OOOO and OOOOa Proposal. Another commenter states that: (1) Methane can be detected more economically than VOC and detecting VOC typically is 2 to 4 times the cost of detecting methane, (2) methane is a reliable indicator of VOC, and (3) detecting methane is safer than detecting VOC. Other commenters disagreed. One commenter states that, while the release of VOC may always be accompanied by methane, it does not follow that the release of methane will always be accompanied by the release of VOC. Some commenters make the case that the NSPS does not simply duplicate requirements for emission controls; rather, it allows, but does not require, operators to comply with both VOC and methane controls using the same practices. Another commenter states that selective technologies do exist and could be applied to reduce VOC but not methane emissions if the methane rescission is finalized. One commenter asserts that it would be arbitrary to regulate methane and VOC as the same just because the currently chosen control technologies are the same. Another commenter adds that, while the sources of VOC and methane leaks may overlap, the two have distinct pollutant effects. The commenter further adds that the urgency and stringency of desired reductions may differ considerably for the two pollutant categories and may change over time, if, for example, the need for climate change mitigation becomes more acute. The commenter suggests that the most sensible approach to regulation of emissions from oil and natural gas operations is, thus, to keep performance standards for both VOC and methane on the books, and to update those standards periodically as the science and technology evolve.

Response: The EPA acknowledges the comments but emphasizes that all of the requirements in the rule apply independently of emissions of either methane or VOC. We discussed this redundancy in detail in section IV.D of the 2019 Proposal (84 FR 50259) and in section V.B of this preamble. The EPA continues to take the position that standards of performance for methane emissions from the production and processing segments are redundant with the existing NSPS for VOC and establish no additional health protections. As explained, every affected source in the production and processing segments will continue to be subject to the same NSPS requirements for VOC as before, and those requirements will have the same impact in reducing the source's methane emissions as before the removal of methane requirements. The EPA maintains that removing the methane NSPS, while retaining the VOC NSPS, will not affect the amount of methane reductions that those requirements will achieve.

One commenter claims that methane can be detected more economically and more safely than VOC. First, it is important to note that BSER for leaking equipment is based on the use of OGI equipment, which does not require the direct measurement of VOC. It is also worthy to note that this commenter was primarily referring to economic and safety advantages of methane leak detection technologies deployed via aircraft, which is not an option currently allowed under the rule.

Comment: One commenter asserts that removing methane standards would almost certainly lead to the adoption of less protective requirements. The commenter notes that in the 2016 Response to Comment Document (p. 2–61), the EPA stated, ''that direct regulation of GHG enables the reduction of additional methane emissions beyond what could be achieved by prior VOC-focused rules.''

Response: The EPA agrees that, in theory, the direct regulation of GHG and consideration of the costs in relation to GHG reduction could result in more stringent standards and more emission reductions than if decisions were made entirely based on VOC emission reductions. The EPA also acknowledges that, for the 2016 Rule, the costs were considered both in relation to the VOC and methane emission reductions. However, the EPA disagrees with the comment that removing methane standards would ''almost certainly'' lead to less protective standards. A separate action amending NSPS subpart OOOOa (EPA–HQ–OAR–2017–0483; FRL–10013–60–OAR; FR Doc. 2020–18115), which will be finalized in the **Federal Register** of Tuesday, September 15, 2020, is an example of how this assertion by the commenter is incorrect.

In 2018, the EPA proposed amendments and clarifications to NSPS subpart OOOOa (83 FR 52056, October 15, 2018) as a result of the reconsideration of issues raised in petitions on the 2016 Rule. In 2018, the EPA proposed to decrease the monitoring frequency for well sites with average combined oil and natural gas production for the wells at the site greater than or equal to 15 barrels of oil equivalent (boe) per day from semi-annually to annually. The EPA also proposed to decrease the monitoring frequency at compressor stations from quarterly to semi-annually. For both of these situations, the standards were both for VOC and methane and the cost-effectiveness based on both VOC and methane emission reductions considered. In fact, the ''multi-pollutant'' cost effectiveness was also considered where the control costs were split between VOC and methane.

In a separate action, the EPA is finalizing the reconsideration amendments to NSPS subpart OOOOa (EPA–HQ–OAR–2017–0483; FRL–10013–60–OAR; FR Doc. 2020–18115). However, the decisions for these reconsideration amendments take into account this final policy review action, which first rescinds the methane standards for production and processing sources. Therefore, the separate reconsideration amendments are finalizing ''VOC-only'' standards based on the cost effectiveness of the reduction in VOC only. These final reconsideration amendments are more stringent than the proposed reconsideration amendments, which were based on both VOC and methane standards. Specifically, in the separate reconsideration action, the EPA is finalizing semi-annual monitoring for well sites with average combined oil and natural gas production for the wells at the site greater than or equal to 15 boe per day and semi-annual monitoring for gathering and boosting compressor stations. Therefore, in this specific situation, the elimination of methane standards resulted in more stringent standards.

Comment: Commenters state that the redundancy rationale does not consider future BSER evaluations required by CAA section 111(b)(1)(B). One commenter notes that CAA section 111(b)(1)(B) requires the EPA to periodically—every 8 years—review and, if appropriate, revise the standards established under this section (we refer to this as the 8-year review). Commenters state that removing methane will mean that the methane requirements will not be subject to this review. One commenter states that the EPA's claimed redundancy ignores that methane regulation will have unique impacts on the 8-year review, including how the Agency considers cost and benefits, which are relevant factors in the likely stringency of the standards the EPA ultimately adopts.

A commenter states that, while the BSER is largely the same for methane and VOC in the current NSPS, there is no guarantee that the BSER will not diverge for the two pollutants in the future. The commenter adds that at least one other GHG—CO_2—is emitted in significant quantities from this industry, and the EPA may determine in the future that it has a rational basis to regulate those emissions under CAA section 111(b). The commenter states that, in that case, the BSER for GHG may differ significantly from the BSER for VOC, since the former would encompass controls for methane and CO_2.

Some commenters remark specifically on the future of technologies for fugitive emission detection and the impact on redundancy. One commenter states that future developments in leak monitoring technology may be able to speciate emissions (*i.e.,* distinguish between methane and VOC), potentially allowing operators to comply with a VOC-only NSPS by controlling VOC while leaving methane emissions unabated. The commenter states that the EPA fails to consider the impact of these VOC-only technologies on future methane emissions in the absence of the current NSPS. Another commenter similarly notes that for newly developed technologies that have the potential to significantly reduce the cost of compliance for regulated entities, the mandates are not redundant. The commenter states that more than 20 percent of natural gas produced in the U.S. has little or no VOC content, making VOC an inherently poor measurement target compared to methane. The commenter adds that some emerging emissions detection technologies—such as spectroscopic sensors used for aerial and satellite surveillance—are more sensitive to methane than to VOC. The commenter adds that, by signaling that reduction of methane emissions is not a national priority, the EPA discourages the development and improvement of the best available controls for methane.

Response: The EPA acknowledges the comments made regarding potential future control technologies and how that could impact redundancy. However, methane and VOC emissions occur through the same emission points and processes, and the same currently available technologies and techniques minimize both pollutants from these emission sources. The EPA recognizes that new control technologies are under development, particularly for detecting fugitive emissions. These emerging technologies include technologies that would detect speciated fugitive emissions from oil and natural gas operations, and, in the 2019 Proposal, the EPA solicited comment on these technologies. 84 FR 50260. We received some information, but we consider it speculative and lacking in specific examples, so that we do not have enough information to evaluate these technologies at this time, much less how these technologies could impact future analyses. In short, the potential for developing future technology that will distinguish between methane and VOC emissions does not change our conclusion that methane requirements at present are redundant. If such technology does develop, the EPA could consider whether to revisit the issue of regulation of methane. By the same token, it is speculative that the 8-year review would result in different levels of controls if EPA were to consider methane emissions and requirements, along with VOC emissions and requirements. In any event, commenters on that review could raise the issue of whether methane should be controlled and whether doing so would result in more stringent VOC controls. With respect to the comment that some natural gas produced has little or no VOC content, the detection of a leak using OGI equipment is not dependent on the relative concentrations of VOC or methane, so that leaks of even low VOC gases would still be identified and required to be repaired. As discussed above, how the emergence of technology in the future could impact the requirements to detect and repair leaks is speculative at this point in time.

The EPA does not agree with the commenter that this action signals a reduction in the prioritization of the reduction in methane. As explained in section V.B.4 of this preamble and above in this section, the methane and VOC requirements are redundant, and the rescission of the methane requirements will streamline the regulation without impacting the methane reductions. With regard to discouraging the development of the best available controls for methane, future evaluations of BSER will continue to recognize the nationwide profile of natural gas, which includes VOC and methane. Therefore, improvements for the control of methane will be considered, as they also will represent improvements for VOC reductions.

Comment: One commenter expresses concern that although methane reductions would still occur even after the EPA rescinds the methane NSPS, the EPA has recently indicated its view that that reductions of co-emitted (but formally unregulated) pollutants should not factor into a benefits analysis in the same manner as those pollutants that are directly regulated. The commenter contends that, under this view, removing methane as a regulated pollutant could result in the Agency disregarding the benefits of methane emission reductions, which the EPA states are the only pollution reduction benefits from the oil and natural gas sector that the EPA can monetize (citing 81 FR 35827, June 3, 2016).

Response: The EPA maintains, as it did at proposal (84 FR 50278), that because the methane control options are redundant with VOC control options in the NSPS subpart OOOOa rule, there are no expected emission impacts or environmental disbenefits from rescinding the methane requirement for the production and processing segments. The EPA has made control decisions on the basis of the cost-effectiveness of the controls, for which monetization of health and environmental impacts other than emission reductions is not necessary. The decision whether to quantify and monetize health and environmental impacts is based upon technical judgments made within the context of developing RIAs which are written to satisfy Executive Order 12866 requirements. The EPA recognizes that in the current previous Oil and Natural Gas NSPS RIAs, the Agency has not quantified the benefits of reductions in emissions other than methane (except for quantifying the amounts of emissions reduced). These RIAs also explained these technical decisions. However, these choices have not influenced the choice of what pollutants to regulate, or the stringency of the standards promulgated, in the Oil and Natural Gas NSPS rulemakings.[71]

Comment: Several commenters state that the EPA fails to identify any way in which the alleged redundancy is problematic. The commenter notes that, while agencies may reconsider and revise their policies, before doing so they must demonstrate ''that the new policy is permissible under the statute, [and] that there are good reasons for it,'' taking into account the record of the previous rule (citing *Fox Television,* 556 U.S. at 515–16). The commenter states

[71] It should be noted that in its recently promulgated rule, ''National Emission Standards for Hazardous Air Pollutants: Coal- and Oil-Fired Electric Utility Steam Generating Units—Reconsideration of Supplemental Finding and Residual Risk and Technology Review'' (signed by the Administrator on April 16, 2020), *https://www.epa.gov/sites/production/files/2020-04/documents/frn_mats_finding_and_rtr_2060-at99_final_rule.pdf,* the EPA based its regulatory decision primarily on the amounts and costs of reductions of the regulated pollutant, but stated that it may continue to consider the co-benefits of reductions in other pollutants, as long as doing so is consistent with the applicable CAA provisions.

that the EPA has failed to provide any ''good reasons'' for why the alleged redundancy between methane and VOC requirements justifies the removal of methane requirements. The commenter explains that the EPA states in the 2019 Proposal that there are ''no expected cost . . . effects from removing the methane requirements . . .'' (citing 84 FR 50247). The commenter states that the EPA characterizes removal of methane requirements as ''less disruptive'' than removal of VOC requirements (citing 84 FR 50260), but does not explain why it is taking any ''disruptive'' action at all, especially since the 2016 Rule has been in full effect and successfully implemented for over 3 years.

Response: The fact that the air pollution controls implemented by sources in the Crude Oil and Natural Gas Production source category to comply with the VOC NSPS reduce methane emissions along with VOC emissions means that the legal requirement to control methane—that is, the methane NSPS—is redundant to the VOC requirement, and, therefore, is unnecessary. The fact that the methane NSPS does not provide benefits—it does not reduce emissions beyond what would otherwise occur—means that the EPA erred in the 2016 Rule when it determined that it had a rational basis to promulgate the methane NSPS, which is sufficient justification to rescind that regulation. As discussed elsewhere, as a predicate for promulgating NSPS for methane, the EPA was required to, and failed, to make a SCF for methane emissions from the appropriately constituted source category.

Comment: One commenter states that the EPA's true rationale for rescinding the methane NSPS is to prevent regulation of existing sources under CAA section 111(d). The commenter notes that the courts have held that administrative agencies must identify their actual reasons for policy choices, that an agency's decision may be arbitrary or pretextual if there is a substantial mismatch between the action and the rationale, and that the courts will compare the evidence for the Agency's decision with the stated explanation to discern whether such a mismatch is present (citing *Dep't of Commerce* v. *New York,* 139 S.Ct. 2551, 2575 (2019)). Noting that CAA section 111(d) imposes, as a precondition to regulation of GHG from existing sources, promulgation of NSPS for GHG under CAA section 111(b), the commenter asserts that in this case, the Agency's true rationale for rescinding the methane NSPS is to prevent regulation of methane emissions from existing oil and natural gas sources under CAA section 111(d). The commenter reviews email communications between oil and natural gas industry officials and EPA (including transition team) officials related to the Agency's decision in early 2017 to rescind the Information Collection Request (ICR) under CAA section 114 for information from existing oil and natural gas sources concerning their methane emissions, coupled with the rescission of that ICR, as evidence of what the commenter considers to be the Agency's true rationale. The commenter asserts that the Agency's stated rationale of redundancy is arbitrary and pretextual.

Response: The EPA disagrees with the commenter. The EPA's reasons for rescinding the methane NSPS are as stated in the 2019 NSPS subparts OOOO and OOOOa proposal, this preamble, and the accompanying documents: The methane NSPS is redundant to the VOC NSPS and does not achieve additional reductions. In other sections of this preamble and the supporting documents, the EPA elaborates upon this rationale and relies on it in responding to adverse comments. The Agency justified its rescission of the ICR in the rulemaking action in which it did so, and that action is separate from this rulemaking.

Comment: Several commenters address the issue of which set of NSPS to retain, methane or VOC. One commenter notes that by keeping the focus on VOC, the EPA ensures that storage tanks, which represent an important source of emissions in the production, gathering and boosting, and processing segments, remain regulated, whereas storage vessels would not be regulated under a methane-only rule. The commenter adds that the EPA data supporting NSPS subpart OOOO shows that, aside from completion activities, estimated VOC reductions from storage vessels represent the largest source of VOC reductions. *See* Regulatory Impact Analysis, April 2012 at Table 3–4. *See* 2019 Proposal, 50260 (''Some sources, such as storage vessels, are subject only to VOC requirements and not methane requirements.''). Other commenters asserted that, if redundancy is the concern for the EPA, the Agency should make methane the key pollutant and remove VOC from the requirements because this will allow for the regulation of existing sources of methane and VOC, and thereby result in reduced environmental, social, and health impacts from both pollutants.

Response: As noted in section V.B above, the EPA is rescinding the methane NSPS and retaining the VOC NSPS, rather than vice versa, because rescinding the latter would affect more facilities, and affect facilities that had been regulated for a longer period. The EPA does not agree that the methane standards should be retained instead of the VOC standards in order to retain the trigger of the CAA section 111(d) requirement to develop standards for existing sources standards. The purpose of the NSPS is to reduce emissions from new sources; as a result, the decision of which NSPS to retain should not turn on the impact on existing sources.

IX. Summary of Significant Comments and Responses on Significant Contribution Finding for Methane

This section summarizes and responds to comments on the 2019 Proposal's solicitation of comment on whether the EPA is required to make, or is authorized to make, a SCF for methane emissions from the Oil and Natural Gas Production source category as a predicate for promulgating methane NSPS.

A. Requirement for Pollutant-Specific Significant Contribution Finding

1. Promulgation of NSPS for Pollutants That the EPA Did Not Evaluate When It Listed the Source Category

Comment: Some commenters assert that CAA section 111 cannot be interpreted to authorize the EPA to promulgate NSPS for air pollutants that were not the subject of the EPA's initial determination that the source category causes or significantly contributes to dangerous air pollution. Commenters argue that in determining which pollutants the EPA should regulate from a source category under CAA section 111(b), it is reasonable to conclude that it should be limited to the pollutants that justified listing that source category for regulation in the first place. Commenters add that this interpretation provides for consistency in applying CAA section 111 across all air pollutants, that is, the EPA regulates air pollutants that it considered when it made a SCF determination for the source category, as well as air pollutants that it regulates subsequently, as long as it makes a similar SCF determination for those subsequently regulated air pollutants. A commenter adds that this approach makes sense because, to list the source category, the Agency must engage in some level of analysis to understand the nature of the emissions from that category; and that the Agency should apply the same analysis to air pollutants that it subsequently seeks to regulate. Numerous commenters state that it is anomalous for the EPA to attempt to regulate methane, as of 2016, based on a SCF determination the EPA made in 1977 and 1978, when methane was not even a regulated pollutant under the CAA.

Other commenters take the opposite view. One asserts that CAA section 111(b)(1) affords the EPA broad discretion to determine which pollutants and sources to regulate and allows the EPA to revise the NSPS to include pollutants or emission sources that were not currently regulated for a particular source category. Other commenters assert that, if the Agency failed to regulate a pollutant emitted from a listed category when it first issued standards for the source category, it must do so in a later rulemaking to achieve the purposes of the CAA, within the limitations set forth in CAA section 111. One commenter argues that CAA section 111(b)(1)(A)'s statutory factors for listing a source category provide a floor according to which the EPA must regulate a particular pollutant from that category, regardless of whether the pollutant is addressed in the initial listing decision.

Response: The EPA agrees that it promotes consistent treatment of all air pollutants subject to the NSPS to require a pollutant-specific SCF as a predicate for regulating a pollutant that the Agency did not consider at the time it made the SCF for the source category and promulgated the initial NSPS. The EPA further agrees that it is anomalous for the Agency to newly regulate an air pollutant, like methane, long after listing the source category on the basis of other pollutants, unless the Agency makes a determination concerning that pollutant that is comparable to the determination that it made when it listed the source category. These considerations support the Agency's interpretation, described in section VI above, that the Agency's authority to promulgate standards of performance for particular air pollutants under CAA section 111(b)(1)(B), along with the definition of ''standard of performance'' under CAA section 111(a)(1), must be interpreted within the context of the finding the Agency makes concerning the source category's contribution to dangerous air pollution under CAA section 111(b)(1)(A). For the same reasons, the Agency disagrees with commenters who assert that listing the source category is a sufficient predicate for subsequent regulation of air pollutants that the Agency did not address in that listing or in promulgating the initial set of standards of performance.

2. Congressional Intent

Comment: The EPA noted in the 2019 Proposal that during the 1977 CAA Amendments, the House-Senate Conference Committee Report described the revisions made to the SCF and endangerment requirements in CAA section 111 and other provisions as follows:

> Provides a uniform standard of proof for EPA regulation of air pollutants which applies to the setting of . . . criteria for national ambient air quality standards under Section 108; . . . new stationary source performance standards under Section 111; . . . new auto emission standards under Section 202; . . . regulations of fuels and fuel additives under Section 211; aircraft emission standards under Section 231.
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> *In all future rulemaking in these areas, the Administrator could regulate any air pollutant from those sources, the emissions of which ''in his judgment cause or contribute to air pollution which may reasonably be anticipated to endanger public health or welfare.''*

H.R. Rep. No. 95–564, at 183–84 (1977) (emphasis added) (cited in 84 FR 50264). The EPA stated in the 2019 Proposal that the emphasized language is evidence that Congress intended to require the EPA (or understood that the EPA had always been required), in promulgating a pollutant-specific NSPS under CAA section 111, to make a pollutant-specific finding, as the EPA does under the other provisions mentioned in the Conference Report. *Id.* at 50264–65.

The 2019 Proposal added that the House Committee Report for the 1977 CAA Amendments included a similar statement in describing one of its purposes for rephrasing the various endangerment finding provisions: ''To provide the same standard of proof for *regulation of any air pollutant, whether that pollutant comes from stationary or mobile sources, or both,* and to make the vehicle and fuel industries equally responsible for cleaning up vehicle exhaust emissions.'' H.R. Rep. No. 94–1175, at 33 (1976) (emphasis added) (cited in *Id.* at 50265). The EPA added that the emphasized phrase could suggest that the House Committee drafters understood the SCF provision in CAA section 111(b)(1)(A) to concern the particular air pollutant subject to the NSPS, like other analogous provisions. *Id.*

Commenters offered competing interpretations of these statements in the 1977 legislative history. Some commenters agreed with the EPA's discussion, noted above. Other commenters, however, state that those Committee Report statements do not support interpreting CAA section 111 to require a pollutant-specific SCF. They assert that the 2019 Proposal was incorrect in suggesting that the 1977 CAA Amendments imposed uniform requirements on the several CAA provisions calling for contribution and endangerment determinations; rather, the commenters noted, the precise terms Congress adopted varied for each of those provisions, the terms function differently for each of the provisions, and the language in the Conference Report was a paraphrase of those provisions. For example, one commenter noted, the statement in the Conference Report does not describe how the cause-or-contribute phrase that appears in section 108 works. The commenter explained that this phrase relates not the to ''the Administrator['s] . . . regulat[ion] [of an] air pollutant from [a] source[ ],'' but instead to the Administrator's decision as to which emissions to include on the list of NAAQS pollutants. The commenter states that the NAAQS program is an area-specific program, not a source-specific one, and it grants states, not the Administrator, the primary authority to directly control emissions to achieve the NAAQS. Other commenters state that the purpose of this language in the Conference Report was to explain that Congress revised the various SCF and endangerment provisions to assure that they were each precautionary, not to assure that they each required a pollutant-specific SCF. Another commenter notes that these revisions to the SCF and endangerment provisions were made to CAA section 111(b)(1)(A), which covers source category listings, but not to CAA section 111(b)(1)(B), which requires the EPA to promulgate standards of performance. The commenter asserts that, if Congress had wanted to make clear that the EPA may not issue standards under CAA section 111(b)(1)(B) unless it had made a pollutant-specific SCF, it could have achieved that result by amending CAA section 111(b)(1)(B) in addition to CAA section 111(b)(1)(A), but it chose not to do so. The commenter asserts that ''[w]hen Congress amends one statutory provision but not another, it is presumed to have acted intentionally'' (citing *Gross* v. *FBL Fin. Servs., Inc.,* 557 U.S. 167, 174 (2009)). Other commenters contend that the Conference Report is at best ambiguous as to whether the source or the air pollutant must be the focus of the ''cause or contribute'' finding, and, in any event, cannot overcome what they describe as the plain meaning of the statute.

Response: We appreciate the different perspectives that commenters provide on the above-quoted statements in the legislative history. Because these statements explicitly describe CAA section 111, along with other CAA provisions, as requiring a pollutant-specific SCF, we think that they can fairly be read to indicate that interpreting CAA section 111 to require, or at least authorize the Administrator to require, a pollutant-specific SCF is consistent with Congressional intent. It was not necessary for Congress to amend CAA section 111(b)(1)(B) explicitly to require a pollutant-specific SCF because its provisions, read in context, already required, or at least authorized the EPA to require, that SCF. None of the commenters point to anything in the legislative history that indicates Congress did not intend to require a pollutant-specific SCF under CAA section 111.

3. Comparison With Other CAA Provisions That Generally Include a Cause or Contribute Finding on a Pollutant-Specific Basis

In the 2019 Proposal, the EPA noted that when Congress enacted CAA section 111 as part of the 1970 CAA Amendments, Congress also enacted several other provisions that required the EPA to promulgate regulations for certain pollutants or certain sources, and that in each of these provisions, Congress required the EPA to make an endangerment or cause or contribute finding, and, further, required the EPA to make the relevant finding on a pollutant-specific basis. The EPA solicited comment on the relevance of whether any of these other provisions for whether CAA section 111 could be interpreted to require, or at least authorize, a pollutant-specific SCF. 84 FR 50263 and 64, 50265 n.74 (discussing, among others, CAA sections 108(a)(1)(A) and (B), 115(a), 202(a)(1), 211(c)(1), 231(a)(2)).

Comment: Some commenters stated that interpreting CAA section 111 to not require a pollutant-specific SCF renders that section anomalous compared with other CAA provisions that premise the EPA's regulatory authority on a pollutant-specific ''cause or contribute'' finding. One commenter suggests that the primary difference between CAA section 111(b) and certain other CAA provisions is that CAA section 111(b) requires that the source category cause or contribute ''significantly'' to air pollution endangering public health or welfare. The commenter states that this implies that the EPA should face a higher burden to justify regulating each specific pollutant under CAA section 111, not a lower burden that allows the EPA to regulate every pollutant from the source category so long as just one meets the statutory criteria.

Other commenters take the opposite position. They assert that the requirements for pollutant-specific cause-or-contribute findings under other CAA sections shows that Congress knew how to require pollutant-specific findings when it intended to do so, and it evidently did not intend to do so under CAA section 111. Another commenter adds that Congress clearly chose to use different phrasing in different sections because it amended all these provisions at the same time in the same section of the 1977 CAA Amendments. From this, the commenter infers that Congress chose to use different phrasing in CAA section 111 than in the other provisions.

One commenter distinguishes CAA section 111 from other CAA provisions that the EPA cited because the latter provisions identify the particular category or class of sources as requiring regulation, and the EPA proceeds to regulate particular pollutants from those sources that it determines cause or contribute to dangerous air pollution. The commenter states that these provisions include CAA section 183(f)(1)(A) (addressing standards applicable to the loading and unloading of tank vessels) and CAA section 213(a)(1) through (4) (governing emission standards for new nonroad engines and vehicles). In contrast, the commenter explains, CAA section 111 does not pre-define any source category for regulation, but instead directs the EPA to fulfill this obligation. The commenter asserts that it is implausible that Congress would rest on any implication from CAA section 111(b) that the EPA must make an additional SCF for each pollutant regulated. The commenter adds that Congress knew how to provide for such an additional finding because CAA section 213(a)(4) requires one for an air pollution problem that (1) emissions from new nonroad engines or vehicles contribute significantly to and (2) emissions from classes or categories of new nonroad engines or vehicles cause or contribute to.

The commenter also identifies another distinction between CAA section 111 and some of the other provisions the EPA cites, which is that the latter address a specific kind or sub-class of pollutants. For example, according to the commenter, CAA sections 108(a)(1)(A) and (B) charges the Administrator with determining which emissions should be classified as criteria pollutants subject to the NAAQS because they contribute to dangerous air pollution and are emitted by numerous diverse mobile or stationary sources, and CAA section 115(a) concerns specific instances in which a pollutant or pollutants that originated in the U.S. cross an international border and endanger public health or welfare in a foreign country. The commenter suggests that a pollutant-specific contribution finding is sensible for these programs: The Agency's task is to identify all the air pollutants that contribute to an air pollution problem in order to determine whether they should qualify as NAAQS pollutants or whether they are harming public health or welfare in another country. The commenter states that this approach is distinct from CAA section 111, which is oriented toward source categories and requires them to achieve an emission limitation that reflects deployment of the BSER for dangerous pollutants, and which does not focus on or even reference any particular type or sub-class of pollutants.

Response: The EPA appreciates the commenters' perspectives on whether the other provisions in the CAA that explicitly require a pollutant-specific contribution finding suggest that Congress did or did not intend that CAA section 111 do so as well. For the reasons described in section VI above, by their terms, CAA section 111(b)(1)(B), in conjunction with CAA section 111(a)(1), and in the context of CAA section 111(b)(1)(A), requires, or at least authorizes the EPA to require, a pollutant-specific SCF as a predicate to promulgating a NSPS for that pollutant, notwithstanding the fact that Congress did not explicitly require such a determination in CAA section 111(b)(1)(B). We believe that this interpretation is consistent with the fact that Congress included requirements for a pollutant-specific cause-or-contribute finding in other CAA provisions. It is true, as the EPA recognized in the 2019 Proposal, 84 FR 50264, and as commenters noted, these other provisions differ from CAA section 111(b) in certain respects, but they differ from each other as well. For example, in CAA sections 213(a)(2), (3), and (4), Congress required a two-step determination, unlike in other provisions. In addition, the fact that CAA section 111 delegates to the EPA the task of identifying the source category for regulation, whereas other provisions themselves identify the source category, explains why it is necessary for the EPA to make a SCF for the source category (it is to assure that the source category merits regulation), but does not provide a compelling reason why the EPA should not also, when it subsequently promulgates a NSPS for a particular pollutant, make a SCF for that pollutant. The important point from comparing these various provisions is that Congress recognized the utility of a pollutant-specific cause-or-contribute finding in a range of circumstances, including a range of regulatory schemes for a range of industries that emit a range of air pollutants that affect a range of geographic areas (including other nations, under CAA section 115). That supports interpreting CAA section 111 to include a pollutant-specific finding as well.

Comment: A commenter asserts that a two-step process in which the EPA makes a SCF for the source category and then for the particular pollutant is anomalous since the other provisions the EPA cites involve only a one-step process. The commenter adds that the two-step process is anomalous because the first step—listing the source category on grounds that it contributes significantly to dangerous air pollution—becomes unnecessary if the EPA must also determine that particular pollutants contribute significantly to dangerous air pollution. The commenter further suggests that a two-step scheme creates two additional anomalies: (1) The EPA might determine that emissions from a source category significantly contribute, but might not be able to determine that any individual air pollutant significantly contributes, and, therefore, might not be able to regulate at all; and (2) the EPA might determine that emissions from a source category significantly contributes, but might be able to regulate only an insignificant portion of those emissions. Another commenter asserts that the other provisions require only a cause-or-contribute finding, not a cause-or-contribute significantly finding, which casts doubt on the EPA's interpretation that CAA section 111(b) requires the latter type of finding.

Response: As noted above, CAA sections 213(a)(2), (3), and (4) impose a two-step process. The commenter's claimed anomalies may be theoretically possible but are highly unlikely to actually occur. The source categories that the EPA lists under CAA section 111(b)(1)(A) are industrial sources that the EPA has determined contribute significantly to dangerous air pollution and that typically emit more than one air pollutant; it is highly unlikely that none of such a category's air pollutants, or only a minor portion of its pollutants, would contribute significantly to dangerous air pollution, and the commenter does not claim that either of those situations is true of any of the some 76 source categories that the EPA has listed. As noted below, the rational-basis approach creates its own set of anomalies. Contrary to the commenter's views, a two-step process under CAA section 111(b)(1), under which the EPA makes a SCF for the source category and a SCF for the particular air pollutants, does not render the first step unnecessary. As the EPA explained in section VI above, the EPA has generally evaluated the contributions of the source category and the air pollutants it emits at the same time, and it has generally relied on data concerning the individual air pollutants to make the SCF for the source category. As a practical matter, then, the EPA generally would need to make a SCF for an air pollutant separately from the SCF for the source category only when the EPA seeks to promulgate a NSPS for an air pollutant that the EPA did not consider when it listed the source category. It is true, as the commenter noted, that the other provisions cited by the EPA in the 2019 Proposal and discussed by the commenters require a pollutant-specific cause-or-contribute finding, and not a SCF, but interpreting CAA section 111(b)(1)(B) to require, or at least authorize the EPA to require, a SCF is consistent with the requirement for a SCF under CAA section 111(b)(1)(A). Section 111(b)(1)(B) of the CAA is not unique in this regard—in the 1990 CAA Amendments, Congress revised the Good Neighbor Provision, CAA section 110(a)(2)(D)(i)(I), to require that SIPs prohibit sources from emitting air pollutants in amounts that will "contribute significantly" to nonattainment downwind.

4. Rational Basis Approach

Comment: Numerous commenters agree with, and elaborate on, the concerns that the EPA expressed in the 2019 Proposal about the rational basis approach (discussed in section VI of this preamble). Some note that the approach is not tied to any language in the CAA, is not based on any statutory criteria, and, thus, is largely undefined. They state that it does not meaningfully limit the EPA's authority and, therefore, injects confusion into the regulatory process. One commenter asserts that it makes no sense to regulate unless there is assurance that the regulation will produce the desired benefits, which may be accomplished only by analyzing emissions on a pollutant-specific basis. Other commenters add that the rational basis standard allows the EPA to rely on a SCF made for a source category decades ago for a different pollutant in order to justify regulating any pollutant from the category—even pollutants that do not cause or significantly contribute to endangerment. Many commenters assert that, without a pollutant-specific SCF, the EPA would have unfettered discretion to add pollutants no matter how minimal the contribution or how benign the impacts to public health and welfare, and that this could result in potentially costly, disruptive, and inefficient regulations on an industry. Another commenter points to anomalies that could result from the rational basis approach: (1) The approach could lead to a case where the EPA would be free to regulate all pollutants from a source category, even though only one of the pollutants was found to contribute to endangerment; and (2) it could result in disparate treatment of similarly emitting source categories: For example, Source Categories 1 and 2 may both emit Pollutant A in equal amounts that do not significantly contribute to endangerment, while Source Category 1 also emits Pollutant B in an amount that does significantly contribute to endangerment. The commenter states that, under the rational basis approach, the EPA would have the authority to list Source Category 1 and regulate emissions of Pollutant A from it, but would not have the authority to list Source Category 2, and, therefore, would not be able to regulate emissions of Pollutant A from it, even though each Source Category's emissions of Pollutant A present identically insignificant risks. The commenter contends that requiring a SCF for each pollutant would prevent these anomalies. In contrast to the vague rational basis standard, other commenters state, CAA section 111(b) provides clear criteria for whether the EPA is authorized to regulate a source's emissions of a pollutant: The endangerment and SCF determinations for listing a source category. Other commenters add that CAA section 111(b) established this rigorous finding as necessary to justify the EPA's authority to promulgate nationwide standards, and that only a pollutant-specific SCF, not a rational basis standard, would maintain that rigorous approach.

Other commenters assert that the requirement of a rational basis standard is appropriate. They note that the standard is equivalent to the "arbitrary and capricious" standard. They state that CAA section 111(b)(1)(A), by its terms, applies the endangerment and SCF findings to the source category as a whole, and not to each newly-regulated pollutant emitted from a previously-listed source category, and that, given that many decisions delegated to the EPA are governed by a default rational basis standard, it is reasonable to conclude that Congress could have intended that standard to govern the regulation of subsequent pollutants from previously-listed sources in the absence of any other prescription for how the EPA is to make the decision. Commenters further state that the arbitrary and capricious standard is not undefined. Rather, one commenter says, the Supreme Court, in defining ''[t]he scope of review under the 'arbitrary and capricious' standard,'' has explained that ''the agency must examine the relevant data and articulate a satisfactory explanation for its action including a rational connection between the facts found and the choice made'' (citing *Motor Vehicle Mfrs. Ass'n of U.S., Inc.* v. *State Farm Mut. Auto. Ins. Co.,* 463 U.S. 29, 42–43 (1983)). The commenter adds that the Court affirmed that it ''may not set aside an agency rule that is rational, based on consideration of the relevant factors and within the scope of the authority delegated to the agency by the statute.'' [72] The commenter adds that this standard applies whether or not Congress has expressly specified the criteria relevant to the Agency's decision. A commenter further notes that under the ''arbitrary and capricious'' standard, the Court has identified certain factors that the EPA must consider in promulgating emission standards under CAA section 111(b) (citing *Sierra Club* v. *Costle,* 657 F.2d 298, 326 (D.C. Cir. 1981). A commenter adds that the Court remanded the Lime Kiln NSPS under the ''arbitrary and capricious'' standard, and quoted from the legislative history of the 1977 Amendments, which indicated Congress's intent that the arbitrary and capricious standard to have teeth: ''With respect to the 'arbitrary and capricious' scope of review retained in these amendments, the conferees intend that the courts continue their thorough, comprehensive review which has characterized judicial proceedings under the CAA thus far'' (citing *Nat'l Lime Ass'n* v. *EPA,* 627 F.2d 416, 452 (D.C. Cir. 1980) (quoting H.R. Conf. Rep. No. 564, 95th Cong., 1st Sess. 178 (1977))). The commenters contend that, under the arbitrary and capricious standard, an EPA decision to promulgate a standard of performance for a benign or harmless substance would fail.

Response: In the 2019 Proposal, the EPA acknowledged that the rational basis test ''offers some protection against arbitrary or capricious decisions by the EPA.'' 84 FR 50263. However, CAA section 111 includes no explicit criteria to guide the application of such a test, and in the times that the EPA has used the test, the EPA has not attempted to articulate criteria or metrics to guide it, and rather, has relied on facts and circumstances. In those respects, the rational basis test is largely (or wholly) undefined and could potentially incorporate a wide range of considerations and lead to inconsistent results. This creates uncertainty for the regulated industry and other stakeholders over whether particular additional pollutants will be regulated or not. The EPA has concluded that the standard is not appropriate for determining the air pollutants for which it will promulgate standards of performance under CAA section 111(b)(1)(B) because of statutory context: CAA section 111(b)(1)(A) makes clear that before the EPA may regulate any air pollutants from major new sources, it must determine that the source category whose sources emit the air pollutants cause or contribute significantly to dangerous air pollution. This is a rigorous predicate for regulation. It is not consonant with this rigorous predicate for the Agency to proceed to regulate the individual air pollutants based only on a rational basis determination. Rather, requiring the Agency to make a SCF determination is consistent with CAA section 111(b)(1)(A). In addition, the SCF determination is better defined because it is focused directly on the extent of the air pollutant's impact on dangerous air pollution, and it provides a metric for assessing that extent: The air pollutant causes or contributes significantly to that air pollution. These metrics more clearly cabin the EPA's discretion.

5. Impacts on the CAA Section 111 Program if a Pollutant-Specific SCF Is Needed

Comment: Commenters state that for more than 4 decades the EPA has interpreted CAA section 111(b)(1) to require a SCF as a prerequisite only for the initial listing of a source category. Commenters contend that, if the EPA now contradicts its past practice and interpretation and undermines or repeals what they describe as the dozens of NSPS it has issued during that time, entities that are subject to new and existing source performance standards under CAA section 111, as well as for the states and local agencies that implement those standards, and other stakeholders, will face regulatory uncertainty and harm to their reliance interests. Commenters add that the EPA's reversal of precedent would also call into question the validity of state implementation plans that were based in part on the continued existence of regulation under CAA section 111(b), as well as the validity of state and Federal plans based on CAA section 111(d) guidelines, and conclude that health and welfare will suffer. Commenters express concern that the EPA fails to provide an analysis of the potential impacts on the overall CAA section 111 program if a pollutant-specific SCF is needed. Commenters assert the EPA should not alter what they describe as the EPA's longstanding interpretation that a pollutant-specific SCF is not needed without first completing a full analysis of impacts such a change would have on existing CAA section 111 rules and soliciting further public participation through a separate notice-and-comment rulemaking process. One commenter contends that, even if the EPA begins requiring a pollutant specific contribution finding, this should not affect the validity of previously, lawfully issued NSPS and CAA section 111(d) guidelines and state plans.

Response: The EPA has listed some 76 source categories and promulgated over 100 standards of performance for them. In the vast majority of cases, the EPA identified the pollutants of concern at the time that it listed the source category or when it promulgated the initial set of standards of performance contemporaneously with the listing or shortly thereafter. It is only in recent rulemakings concerning GHG that stakeholders have expressed concerns that the EPA had not considered GHG when listing the source category, and, thus, had not made determinations for GHG consistent with the determinations that the EPA made to justify regulation of other pollutants from the source categories. Accordingly, the EPA disagrees with commenters who are concerned that interpreting CAA section 111 to require a pollutant-specific SCF will undermine numerous NSPS, with adverse effects for other CAA control programs. In addition, the rational basis approach, under which the EPA promulgates a standard of performance for a pollutant upon determining that it has a rational basis for doing so, cannot be considered to be long-established. The EPA clearly articulated this standard for the first time to justify regulation of a previously unregulated

[72] By the same token, a commenter notes that the EPA explained the rational basis test in its response to comments on the 2016 Rule as follows: ''the EPA's use of the phrase 'rational basis' . . . explains how the agency's actions are supported by the record and is a reasonable exercise of the EPA's broad authority under section 111'' (citing the EPA's Response to Public Comments at 2–16, Docket ID Item No. EPA–HQ–OAR–2010–0505–7632 (May 2016).

air pollutant in the 2015 EGU GHG NSPS rule, and then again in the 2016 Rule. The EPA considers that the present rulemaking has provided a full opportunity for the public to respond to the solicitation of comment on the pollutant-specific SCF interpretation.

B. Significant Contribution Finding in 2016 Rule

1. 2016 SCF for Methane Emissions From the Oil and Natural Gas Source Category

Comment: Several commenters contend that oil and gas methane emissions are too small to be considered ''significant.'' These commenters cite as support that the contribution of oil and gas to total U.S. GHG emissions is only 3 percent, that U.S. methane emissions are only 7 percent of global methane emissions, that U.S. methane emissions are only 1 percent of global GHG emissions, and that estimated impacts of the 2016 Rule would be to reduce methane concentrations in 2100 by 0.12 percent and temperatures by less than a thousandth of a degree. Other commenters assert that, if a SCF for methane emissions from the Oil and Natural Gas source category were required under the statute, the EPA fully satisfied this obligation in the 2016 Rule. Several commenters assert that, even if the EPA eliminates the transmission and storage segment from the source category, the 2016 SCF remains appropriate and binding. A commenter notes in the 2019 Proposal the production and processing segments account for 1.8 percent of global methane and 0.3 percent of total global GHG and states this is equal to or greater than the total methane emissions from all but eight countries around the world. The commenter asserts that these totals are significant by any measure. One commenter states that because climate change is a global phenomenon, small percentage changes are relevant and addressing a large number of smaller sources will ultimately reduce the rate of climate change. The commenter adds that to solve a global problem, reductions of a fraction of a percent are substantial and important (citing 2016 Rule's Response to Comments Document, Docket ID Item No. EPA–HQ–OAR–2010–0505–7632). One commenter states that, if the production and processing segments were listed as an individual methane source, it would still be larger than every other source currently listed apart from enteric fermentation. One commenter notes that in light of methane's 20-year GWP of 87, methane from the domestic sources accounts for 9.3 percent of total U.S. GHG emissions and 1.2 percent of global GHG emissions. One commenter states that the transmission and storage segment emits 16.8 percent of the source category's total GHG emissions and it would be arbitrary and capricious for the EPA to undermine its 2016 SCF by removing from that source category facilities that emit only a minority of the pollutants.

Response: The EPA agrees with commenters that the 2016 Rule failed to provide a pollutant-specific SCF as a prerequisite to imposing NSPS regulations for methane emissions. The SCF determination made in the 2016 Rule was on the basis of methane emissions from the production, processing, transmission and storage segments. In this action, the EPA is removing the transmission and storage segment from the source category. The 2016 Rule did not assess whether methane emissions from the production and processing segments alone cause or contribute significantly to dangerous air pollution; thus, we find that the 2016 Rule's determination is not adequate. In addition, the EPA has yet to makes an appropriate determination that methane emissions from the Oil and Natural Gas Production source category cause or contribute significantly to dangerous air pollution. The EPA appreciates the commenters' views concerning the amounts and impacts of methane emissions from the transmission and storage segment, as well as the production and processing segments, but until the EPA itself reviews and assesses those amounts of emissions, it cannot make a determination as to whether methane emissions from the production and processing segments contribute significantly to dangerous air pollution.

2. Identification of the Standard for Determining Significance

Comment: Commenters responded to the EPA's solicitation of comment concerning whether, as a matter of law, under CAA section 111, the EPA is obligated to identify the standard by which it determines whether a source category's emissions contribute significantly, and whether, if not so obligated, the EPA nevertheless fails to engage in reasoned decision-making by not identifying that standard. Some commenters stated that the EPA must identify the standard by which it determines whether a source category's emissions ''contribute significantly.'' They asserted that, in order to not be arbitrary and capricious, an agency must articulate a reasonable explanation for the actions it takes, and that as a result, the EPA should establish what constitutes ''significant'' contribution for purposes of CAA section 111(b). They note that the EPA has done so for other programs that require a similar showing, such as CAA sections 110(a)(2)(D)(i), 189(e), and 213 (citing 76 FR 48208, 48236 and 37 (August 8, 2011) (Cross-State Air Pollution Rule)). Other commenters assert there is no indication that Congress intended that the EPA must establish such a standard before making a SCF and that the EPA has made SCFs for dozens of source categories over almost 50 years without having established such a standard. They added that in the past, the EPA has appropriately relied on a facts and circumstances analysis and that it would be irrational to adopt a standard or threshold because different air pollutants have different effects on health and/or welfare, as well as different geographic trajectories.

Response: The EPA appreciates these comments, as well as the additional ones noted in the Response to Comments Document. They will inform the Agency's future consideration of this issue. As explained above, the Agency has concluded that it must identify a standard for ''contribute significantly'' in order to make a SCF for a source category, to ensure not only that the public is on notice of the criteria that the Agency uses in making such determinations but also that the Agency itself is acting consistently in making such determinations. However, it is not necessary to resolve the specific content of this standard in this rulemaking because, as discussed above in section VI of this preamble, the EPA is rescinding the SCF for methane from the Oil and Natural Gas Production source category that the Agency made in the 2016 Rule, on the ground that the scope of the source category inappropriately included the transmission and storage segment.

C. Criteria for Making a Significant Contribution Finding Under CAA Section 111

Comment: Several commenters responded to the EPA's solicitation of comment regarding criteria for the EPA to consider in making a SCF. Some recommend that the EPA defer any action on SCF criteria and instead address this question in a future advance notice of proposed rulemaking, ICR, and/or proposed rulemaking. One commenter adds that deferring the issue would allow the EPA to focus on finalizing the core rulemaking and to streamline issues in any future legal challenge to a final rule. Some commenters discuss other contexts under the CAA in which the Agency has interpreted and applied similar language to governing the SCF determinations under CAA section 111(b)(1)(A). For example, these commenters discuss factors suggested by past EPA action under CAA sections 189(e) and 213(a)(2), (3), and (4). Some commenters suggest specific criteria that the EPA could consider, including, among others, consideration of the 1979 source category listing methodology, factors related to climate change, all factors relevant to a source category's contribution on a case-by-case basis, accumulation in the atmosphere of pollutants, projected future emissions, and consistency with the goal of protection of the Nation's air resources. We summarize these comments at greater length in the Response to Comments Document.

Response: The EPA acknowledges the commenters' statements. As pointed out in the proposal, the EPA does not intend for these comments to inform the finalization of this rule, but rather to inform the EPA's actions in future rules. Therefore, the EPA is not evaluating the merits of comments on these topics at this time. However, the Agency will look at the details provided in these comments when considering future action in making a SCF.

X. Summary of Significant Comments and Responses Concerning Implications for Regulation of Existing Sources

A. Existing Source Regulation Under CAA Section 111(d)

Comment: Several commenters agree with the statements in the 2019 Proposal that the EPA's rescission of the applicability of the NSPS to methane emissions for the sources in the Crude Oil and Natural Gas Production source category that are currently covered by the NSPS would have the consequence that the EPA would no longer be authorized to regulate existing sources of the same type in the source category under CAA section 111(d).

However, other commenters assert that the 2016 Rule regulation of methane from the oil and natural gas sector has already triggered a mandatory duty for the EPA to develop CAA section 111(d) EG for existing sources within that sector. They state that the EPA's 2009 endangerment finding for GHG emissions and its 2016 rational basis determination and pollutant-specific endangerment/SCF for methane emissions from the Oil and Natural Gas Production source category obligate the EPA to regulate such emissions not just from new sources under CAA section 111(b), but also from existing sources under CAA section 111(d).

Response: The EPA agrees that following promulgation of the methane NSPS in the 2016 Rule, the EPA was obligated to develop EG under CAA section 111(d) for existing sources of methane in the source category. However, that obligation ends with the rescission of those NSPS. Section 111(d)(1) of the CAA provides by its terms that the EPA is authorized to promulgate guidelines for regulation of any existing source ''to which a standard of performance under this section would apply if such existing source were a new source.'' Once the EPA has rescinded the methane NSPS, existing sources of methane would no longer be subject to such an NSPS if they were new sources. As a result, from the time of the rescission forward, the EPA would no longer have authority to promulgate guidelines to regulate those sources. Nothing in CAA section 111(d) indicates that once the EPA promulgates NSPS that trigger an obligation to regulate existing sources, that obligation remains in place even after the NSPS has been rescinded.

Comment: As discussed in the proposal preamble for this action, the EPA interprets CAA section 111(d) as not permitting a CAA section 111(d) existing source regulation to be developed as a result of the NSPS for VOC emissions from new sources in the Crude Oil and Natural Gas Production source category under CAA section 111(b). Specifically, the EPA stated that VOC do not qualify as the type of air pollutant that, if subjected to a standard of performance for new sources, would trigger the application of CAA section 111(d) the pollutants excluded from regulation under CAA section 111(d) include pollutants which have been included on the EPA's CAA section 108(a) list. VOC are not expressly listed on the EPA's CAA section 108(a) list, but they are precursors to ozone and PM, both of which are listed CAA section 108(a) pollutants. The definition of ''air pollutant'' in CAA section 302(g) expressly provides that the term ''air pollutant'' includes precursors to the formation of an air pollutant ''to the extent that the Administrator has identified such precursor or precursors for the particular purpose for which the term 'air pollutant' is used.'' Based on this ''particular purpose'' phrasing, it is appropriate to identify VOC as a listed CAA section 108(a) pollutant for the particular purpose of applying the CAA section 108(a) exclusion in CAA section 111(d) [hereinafter referred to as the EPA's ''VOC exclusion argument'']. 84 FR 50272. Comments provided on the proposal both agree and disagree with this interpretation. These comments are provided below.

Commenters that agree with the EPA's interpretation assert that the statute is clear that a source category cannot be subject to CAA section 111(d) emission standards for ''any pollutant . . . for which air quality criteria have . . . been issued or which is . . . included on a list published under'' CAA section 108(a). The commenters state that while VOC are not themselves directly on the list of criteria pollutants under CAA section 108, the EPA has designated them as precursors for ozone and PM, both of which are listed CAA section 108(a) criteria pollutants. The commenters add that the CAA defines ''air pollutant'' to include ''any precursors to the formation of any air pollutant, to the extent the Administrator has identified such precursor or precursors for the particular purpose for which the term 'air pollutant' is used,'' and because the ''particular purpose'' of the term ''air pollutant'' in CAA section 111(d) is to identify pollutants that are already subject to regulation under the NAAQS program, it is appropriate to conclude that VOC are one of the ''air pollutants'' covered by this exclusion.

Conversely, several other commenters disagree with the EPA's interpretation that CAA section 111(d) does not require that existing source regulation be developed as a result of the NSPS for VOC emissions from new sources in the Crude Oil and Natural Gas Production source category under CAA section 111(b). One commenter notes that the EPA first argues that VOC are ''regulated under the CAA's NAAQS/SIP program'' because they are precursors to listed pollutants ozone and PM, pointing to provisions of the CAA relating to requirements for ozone non-attainment areas that explicitly call for reductions in VOC emissions. The commenter asserts, however, that the statutory test for whether a pollutant is excluded is not whether it is ''regulated under'' CAA section 108 or CAA section 110, but rather the test is whether air quality criteria have been issued for the pollutant of concern, or the pollutant has been listed under CAA section 108. The commenter asserts that neither of these is true here for VOC, as the only pollutants for which air quality criteria have been issued or included on a list published under CAA section 108(a) are SO_2, PM_{10} and $PM_{2.5}$, CO, ozone, NO_X, and lead.

One commenter contends that the proposal VOC exclusion argument contradicts the Agency's own position in other regulations and notes that in 1996 the EPA finalized parallel rulemakings for new and existing municipal solid waste (MSW) landfills under CAA sections 111(b) and 111(d), respectively. The commenter states that pollutants deemed harmful to human health emitted from MSW landfills included methane, VOC, HAP, and odorous compounds, collectively termed ''landfill gas.'' The commenter notes that the EPA chose to use non-methane organic compounds (NMOC), which includes VOC, as a surrogate for landfill gas in its setting standards of performance and EG for new and existing MSW landfills under CAA sections 111(b) and 111(d). The EPA updated these regulations in 2016 (2016 Standard), with its new EG ''expected to significantly reduce emissions of LFG [landfill gas] and its components, which include methane, VOC, and hazardous air pollutants (HAP).'' The commenter states that the EPA noted that reducing methane had become more important since the prior 1996 rulemaking, which had focused on NMOC (including VOC) ''because NMOC contain[ed] the air pollutants that at that time were of most concern due to their adverse effects on public health and welfare.'' The commenter adds that, as such, the 2016 Standard was focused on ''reducing [both] the NMOC and methane components of LFG.'' The commenter provides that the EPA acknowledged VOC was a precursor to criteria pollutants $PM_{2.5}$ and ozone, but nowhere did the EPA make the argument the Agency now raises that VOC status as a precursor means that it is not subject to regulation under CAA section 111(d).

Response: First, with respect to the comment that the EPA has applied a ''regulated under CAA 108'' test rather than the ''listed under CAA 108'' test that is stated in the statute, this comment misstates the EPA's argument. The EPA's conclusion is that VOC are included within the CAA section 108(a) listings for ozone and $PM_{2.5}$ for the particular purpose of applying the CAA section 108(a) exclusion in CAA section 111(d). The ''regulated under CAA 108'' point is one of the reasons why the EPA has concluded that it is appropriate to consider VOC to be part of the CAA section 108(a) listings for ozone and PM 2.5 for this purpose—because VOC are regulated through the NAAQS implementation program, and thus there is no gap in the CAA regulation of VOC that needs to be covered by CAA 111(d) regulation. In other words, we are not concluding that VOC are excluded from CAA 111(d) regulation because they are regulated under the NAAQS implementation program. Instead, we are concluding that VOC are excluded from 111(d) regulation because they are part of the CAA 108(a) listings for ozone and $PM_{2.5}$ for the purpose of applying CAA section 111(d), and we reach that conclusion based in part on the fact that VOC are regulated through the NAAQS implementation program.

Second, the argument that EPA's regulation of municipal solid waste (MSW) landfill emissions (sometimes referred to as ''landfill gas'') under CAA 111(d) contradicts EPA's conclusion that VOC cannot be regulated under CAA 111(d), because MSW landfill emissions landfill includes VOC among its components, is incorrect. The EG and standards of performance for MSW landfills that were originally promulgated in subparts Cc and WWW of part 60 and subsequently in subparts Cf and XXX regulate only ''MSW landfill emissions,'' not the individual components of landfill gases. *See* 40 CFR 60.30c through 60.36c; 40 CFR 60.30f through 60.41f; 40 CFR 60.750 through 60.759, and 40 CFR 60.760 through 60.769. Both the regulatory text in these subparts and the EPA's preamble discussion explicitly address this issue and clarify that ''MSW landfill emissions'' is a single designated pollutant and the only pollutant subject to regulation by these subparts.

For example, the regulatory text of 40 CFR part 60, subpart Cc, clarified that it contains guidelines for the control of ''certain designated pollutants'' and identifies ''MSW landfill emissions'' as the pollutant to be controlled by the state plans. 40 CFR 60.30c and 60.33c(a). The same is true for 40 CFR part 60, subpart Cf. 40 CFR 60.30f (subpart establishes requirements for ''designated pollutants), 60.33f(a) (pollutant to be controlled is ''MSW landfill emissions''). Similarly, 40 CFR part 60, subparts WWW and XXX, require affected sources to collect and control landfill gases, and each defines ''MSW landfill emissions'' as ''gas generated by the decomposition of organic waste deposited in an MSW landfill or derived from the evolution of organic compounds in the waste.'' 40 CFR 60.751; 40 CFR 60.761. This definition in each subpart makes clear that the regulated pollutant is confined to emissions that originate from an MSW landfill.

Further, in proposing the MSW regulations in 1991, the EPA was explicit that it was regulating only MSW landfill emissions collectively, and not the individual components of those emissions. The EPA stated the following in the preamble to the proposed rule:

> The pollutant to be regulated under the proposed standards and guidelines is ''MSW landfill emissions.'' Municipal solid waste landfill emissions, also commonly referred to as ''landfill gas,'' is a collection of air pollutants, including methane and NMOC's [non-methane organic compounds], some of which are toxic. The composite pollutant is proposed to be regulated under section 111(b), for new facilities, and is proposed to be the designated pollutant under section 111(d), for existing facilities.

56 FR 24468, 24470 (May 30, 1991). In additional discussion, the EPA explained the following:

> The EPA views these emissions as a complex aggregate of pollutants which together pose a threat to public health and welfare based on the combined adverse effects of the various components. . . . [T]he exact composition of MSW landfill emissions can vary significantly from landfill to landfill and over time. Although the types of compounds are typically the same, the complex mixture cannot be characterized quantitatively in terms of single pollutants. The EPA thus views the complex air emission mixture from landfills to constitute a single designated pollutant.

Id. at 24474–24475. Thus, the argument that VOC or any other of the individual components of landfill gases are separately regulated under these provisions is incorrect and inconsistent with the regulatory text and record for these subparts.

Comment: The proposal preamble for this action cited CAA section 112(b)(2) and argued that the ''except'' phrasing of CAA section 112(b)(2) suggests that air pollutants which are ''listed under section 7408(a)'' can be read to include precursors to the pollutant that is listed under CAA section 108(a). The EPA provided that otherwise the pollutants that are described in the second part of the sentence (pollutants that meet the listing criteria and are precursors to a CAA section 108(a) pollutant) would not be an exception to the prohibition in the first part of the sentence. 84 FR 50272.

One commenter contends that the EPA's analogy to CAA section 112 to ostensibly demonstrate that Congress would have explicitly subjected precursors to regulation in CAA section 111(d) if it wanted to, because it did so in CAA section 112 is inapposite here. The commenter states that, first, as the EPA acknowledges, Congress provided a flexible definition of ''air pollutant'' depending on ''the particular purpose for which the term 'air pollutant' is used.'' The commenter states that the particular purpose for which the term ''air pollutant'' is used in CAA section 112 is quite different than in CAA section 111(d). The commenter notes that the relevant statutory provision in

CAA section 112 excludes from regulation as a HAP any ''air pollutant[s] listed under section [108(a)] . . . except that . . . precursor[s] to a pollutant which [are] listed under section [108(a)]'' can be regulated as a HAP. The commenter states that the EPA argues that to interpret the phrase ''air pollutant[s] listed under section [108(a)]'' as being exclusive of precursors would render meaningless the exception in CAA section 112(b)(2) for precursors. The commenter contends that it may be true in the context of CAA section 112, but it does not follow that the same interpretation applies in CAA section 111, which lacks such an express statutory exception.

Response: This commenter misunderstands the relevance of the text in CAA section 112(b)(2) in determining whether VOC are excluded from CAA section 111(d) regulation by the CAA section 108(a) exclusion. The EPA is not drawing an analogy to the outcome in CAA section 112(b)(2), which expressly removes precursors from the prohibition on the regulation under CAA section 112 of air pollutants listed under CAA section 108(a). The point here is that CAA section 112(b)(2) demonstrates that Congress understood that the phrase ''air pollutant listed under section 7408(a)'' could be read to encompass precursors. Moreover, in CAA section 112(b)(2) Congress included express language stating its choice: That regulation of precursors under CAA section 112 was not barred by the prohibition on regulating pollutants listed under CAA section 108(a). In CAA section 111(d), however, Congress did not state a choice; it stated an exclusion for pollutants listed under CAA section 108(a) without specifying whether that exclusion extended to precursors. This ambiguity, combined with the CAA section 302(g) definition of ''air pollutant'' that expressly gives the EPA the discretion to determine whether precursors are to be considered part of ''air pollutant'' on a case-by-case basis for each ''particular purpose for which the term 'air pollutant' is used,'' means that the EPA has to apply its expertise in administering the CAA program to determine whether the air pollutants excluded from CAA section 111(d) regulation by the CAA section 108(a) exclusion covers precursors. For all of the reasons discussed, the EPA has reasonably concluded that precursors are excluded by the CAA section 108(a) exclusion.

Comment: The proposal preamble for this action stated that ''CAA section 111(d) is properly understood as a 'gap-filling' measure to address pollutants that are not addressed under either the NAAQS/SIP provisions in CAA sections 108–110 or the HAP provisions in CAA section 112. Because VOC are regulated as precursors to ozone and $PM_{2.5}$ under CAA sections 108–110, they are properly excluded from regulation under CAA section 111(d) because the ''gap-filling'' function of CAA section 111(d) is not needed.'' 84 FR 50272. Some commenters agreed with the EPA's interpretation that CAA ''section 111(d) is properly understood as a 'gap filling' measure to address pollutants that are not addressed under either the NAAQS [SIP] provisions in CAA sections 108–110 or the [HAP] provisions in CAA section 112.'' These commenters generally note that regulation of existing sources under CAA section 111(d) is very rare and that the provision has been used only a handful of times, in part because it can only be triggered by a handful of pollutants and that Congress' inclusion of CAA section 111(d) can only be viewed as a safety valve for a limited number of circumstances. One commenter concludes that because VOC emissions are regulated under CAA section 108 and related statutory provisions as part of the NAAQS implementation program, they do not fall into this ''gap'' and cannot be regulated under CAA section 111(d).

Conversely, other commenters assert that the EPA's proposal preamble discussion regarding CAA section 111(d) as a gap-filling measure does not support the EPA's claim that Congress intentionally chose to exclude criteria pollutant precursors from regulation under CAA section 111(d) and that the ramifications of such an interpretation would be enormous.

The commenter states that the EPA makes a structural argument that excluding VOC from regulation under CAA section 111(d) makes sense with respect to that section's ''gap-filling'' role, since VOC are already ''regulated as pre-cursors under CAA sections 108–110'' and, thus, there is no gap to be filled. However, the commenter believes that this argument ignores the legislative history of CAA section 111(d). The commenter asserts that CAA section 111(d) began as a Senate proposal with an explicit list of pollutants to be regulated, and that ultimately, this explicit list was replaced with gradually broader phrasing until the language we see today was included in the 1970 CAA Amendments. The commenter adds that the legislative history reflects Congress' intent to give the EPA the flexibility to regulate a broad range of pollutants, rather than to constrain the EPA's discretion to a designated list of pollutants subject to regulation under CAA section 111(d). The commenter contends that the EPA's current interpretation would restrict the applicability of CAA section 111(d) to a narrower set of pollutants than Congress intended, and indeed, to a narrower set of pollutants than the Agency itself has regulated in the past. The commenter concludes that contrary to the EPA's assertions in its proposal, such a narrow interpretation upends the very idea of a ''gap-filling'' provision intended to give the Agency the flexibility to regulate a broad range of pollutants where necessary to fill gaps left by the NAAQS and NESHAP programs.

Response: The EPA disagrees with this comment. First, the argument that legislative history shows that Congress intended to give the EPA the authority to regulate a broad range of pollutants under CAA section 111(d) fails in the face of the statutory exclusions of pollutants that Congress enacted. The exclusions in CAA section 111(d) expressly narrowed the breadth of the pollutants that the EPA can regulate under CAA section 111(d). Second, the gap-filling role of CAA section 111(d) is properly understood to fill the gaps that exist *between* the regulatory regimes that address criteria/CAA section 108(a) pollutants and HAP—that is, the regulation of those pollutants that are not listed and regulated under those other CAA programs. CAA section 111(d) is not properly read to fill gaps that exist *within* those other CAA programs.

B. Impact of Lack of Regulation of Existing Oil and Natural Gas Sources Under CAA Section 111(d)

In the proposal preamble, the EPA stated that ''the lack of regulation of existing sources under CAA section 111(d) will not mean a substantial amount of lost emission reductions.'' 84 FR 50271. The proposal preamble provided several reasons for why there could be limited impact from not regulating existing oil and natural gas sources under CAA section 111(d), including (1) equipment turnover/source modifications will result in existing sources being subject to the NSPS, (2) market incentives capture valuable methane product, (3) voluntary actions to reduce methane emissions are prevalent, and (4) state regulations result in emission reductions. The EPA received comments that both agree and disagree with the EPA's conclusions and reasoning presented in the proposal preamble. These comments and the EPA response to their comments are provided below.

Comment: Several commenters assert that the EPA's assertion that the lack of regulation of existing sources directly caused by the proposed rule to deregulate methane emissions from new sources will have ''limited impact,'' does not have sufficient supporting data or analysis, and is false and arbitrary and capricious. One commenter states that, although the EPA attempts to downplay the likely impact from its non-regulation of existing sources, the EPA fails either to define what it means by ''substantial'' or to provide evidence to support this claim.

The commenters state that it would not be rational or legal for the EPA to put blinders on in order to ignore the enormous consequences of rescinding methane regulation for existing sources. The commenters assert that section 111 of the CAA is concerned with reducing dangerous pollution from stationary sources—new, modified, and existing. *See, e.g.,* 42 U.S.C. 7411(b)(1)(B) (discussing ''new sources within such category''); *Id.* 42 U.S.C. 7411(d)(2)(B) (discussing existing sources as ''sources in the category of sources''). Some commenters state that while the EPA claims that ''[a]nalysis of potential impacts of removing the requirement to regulate existing sources under CAA section 111(d) is outside the scope . . . and would be speculative,'' the EPA's refusal to consider these impacts renders its proposal unlawful.

Response: The EPA acknowledges in the proposal preamble (84 FR 50271) that by rescinding the applicability of the methane NSPS for the sources in the Crude Oil and Natural Gas Production source category, existing sources of the same type in the source category will not be subject to regulation under CAA section 111(d). The EPA is not required under a CAA section 111(b) NSPS subpart OOOOa rulemaking, however, to consider the impacts of existing sources not being regulated under a hypothetical CAA section 111(d) rule as a result of amending a CAA section 111(b) rule. While the EPA did not prepare and include a quantitative analysis that estimates the levels at which source modification/equipment turnover, market incentives, voluntary programs, and state requirements—might limit potential emissions increases from not regulating existing sources, the EPA discusses how each of these factors currently contribute and will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources in absence of an EG in absence of existing source CAA section 111(d) guidelines.

The EPA concedes, however, that the use of the term ''substantial'' conveys a quantitative value, and that it would have been more accurate in absence of a quantitative analysis to state that these factors all have the potential to motivate or require operators to control emissions from existing sources in absence of a CAA section 111(d) EG. Further detail regarding comments received on the potential for limiting emissions from existing sources for each of these factors, and responses to these comments are provided below.

Comment: Several commenters suggest that the EPA's claim that equipment turnover, market incentives, voluntary actions, and state regulations will mean that there will not be a substantial loss of emission reductions is inconsistent with findings the EPA itself made in prior rulemakings, including the 2016 Rule. The commenters state that the EPA has provided no rational basis for its drastic shift in position (citing *Lone Mountain Processing, Inc.* v. *Secretary of Labor,* 709 F.3d 1161, 1164 (D.C. Cir. 2013)).

Response: The EPA's notes that changes have occurred since the earlier rulemakings that affect emissions from existing oil and natural gas sources. For example, there is greater industry participation in voluntary methane emissions reduction programs/actions and more state regulations/permits limiting emissions from oil and natural gas operations than there were when the EPA developed the 2016 Rule.

Comment: Commenters contend that the EPA cannot support not establishing standards under CAA section 111(d) based on source modification/ equipment turnover, market incentives, voluntary programs, or state requirements factors mitigating potential emissions increases from not regulating existing sources. The commenters note that the cited factors are precisely the ones that Congress rejected when it chose to require uniform national standards. The commenters also note that the CAA is clear: The EPA ''shall prescribe regulations'' for existing sources in listed source categories that are subject to new source requirements for air pollutants not regulated under the NAAQS or section 112. 42 U.S.C. 7411(d)(1). The commenters suggest that the EPA's reliance on source modification, market incentives, voluntary programs, and state requirements to justify the proposal exceeds the Agency's authority under the CAA (citing *Massachusetts* v. *EPA,* 549 U.S. 497, 533–535 (2007) (the EPA cannot rely on a ''laundry list of reasons not to regulate'' when there is a ''clear statutory command'' under the CAA)).

Response: The EPA recognizes that rescinding the applicability of the NSPS to methane emissions for the sources in the Crude Oil and Natural Gas Production source category that are currently covered by the NSPS will mean that existing sources of the same type in the source category will not be subject to regulation under CAA section 111(d). The reasoning for not developing a CAA section 111(d) standard is not because source modification, market incentives, voluntary programs, and state requirements will limit emissions increases that may result from not pursuing a CAA section 111(d) standard. Rather, this is a legal consequence that results from the application of the CAA section 111 requirements.

Comment: Several commenters specifically provide support for, and opposition to, the individual factors (equipment turnover/source modifications, market incentives, voluntary actions, and state regulation) cited by the EPA as mitigating emission increases as a result of not regulating existing sources.

Equipment turnover/source modifications. One of the factors that the EPA provided in the proposal for the limited impact of the lack of regulation of existing sources under CAA section 111(d) was ''that the number of existing sources may decline over time due to obsolescence or to shut down and removal actions.'' 84 FR 50273. The EPA provided analysis to support this rationale and also solicited comment regarding the rate at which this decline can be expected to occur. One commenter supported the proposal by stating that because CAA section 111 defines an ''existing source'' as one that is not a ''new source,'' the universe of existing oil and natural gas sources potentially subject to CAA section 111(d) requirements would be any affected facility for which construction commenced on or before September 18, 2015, indicating that any ''existing source'' has already been in operation for at least 4 years. The commenter contends that even if the EPA were to issue EG for methane for these sources today, the Agency's 40 CFR part 60, subpart Ba regulations implementing CAA section 111(d) (Emission Guidelines for Municipal Solid Waste Landfills) provide states with 3 years to develop and submit their state plans. The commenter notes that these state plans may provide a source with up to 24 months to comply with emission standards (or longer if the compliance schedule includes legally enforceable increments of progress), and states retain discretion under CAA section 111(d) and the regulations to further extend these compliance deadlines for an individual source based on its remaining useful life or other factors. The commenter states that by the time CAA section 111(d) emission standards would become effective, roughly 10 years will have passed since the date marking the cutoff between ''new'' and ''existing'' sources. During that time period, the commenter states, it is likely that sources constructed before this cutoff will have been plugged and abandoned or replaced with new equipment that would itself be subject to the VOC requirements of NSPS subpart OOOO (which will also reduce associated methane emissions). The commenter adds that those existing oil and natural gas sources that are not plugged and abandoned or replaced may also undergo changes that qualify as ''modifications'' under NSPS subpart OOOOa, and in that case would be treated as new sources.

Conversely, several other commenters express concern that the EPA has not supported its claim that source turnover is one reason for the limited impact of not regulating existing sources. One commenter contends that the EPA's withdrawal of the ICR, coupled with its lack of information that could support a reasoned analysis, makes its action arbitrary and capricious. One commenter notes that the average life of an oil and natural gas well is 20 to 30 years, meaning that facilities installed prior to September 2015 could still be in operation in September 2045. The commenter points out that many of the largest-emitting facilities (*e.g.,* field storage tanks) typically do not undergo modification or reconstruction during their useful life.

Another commenter asserts that the EPA's claim that the existing source inventory will turn over is undercut by the EPA's extensive list, in the 2019 Proposal preamble, of questions to stakeholders about the rate of modification practices within the sector. The commenter states that the existence of the EPA's extensive list of questions indicates that the EPA has little information on how regularly these transitions occur and cannot claim that there will be little emissions impacts until after the Agency has analyzed the information that it requests.

Some commenters assert that the EPA-cited data from the U.S. Greenhouse Gas Inventory (GHGI) (for pneumatic controllers, compressors, tank throughput, and well completions); *Drillinginfo.com* (for well completions); and NSPS subpart OOOOa compliance reports (for assessing turnover rates) do not support the EPA's turnover conclusions, and exhibit substantial limitations for assessing turnover and obsolescence rates. For example, the commenters note that the GHGI provides absolute source counts for each year, but does not include information on specific sources—meaning it is not possible to assess the number of sources that are new, the number that have ceased operation, or the number that have remained in use over a time period.

Furthermore, the commenters contend that the EPA's analysis ignores large sources of emissions, such as reciprocating compressors and all leaks downstream of well pads. The commenters address the data the EPA provided by source (*i.e.,* pneumatic controllers, compressors, storage vessels, well completions) to illustrate their point that the data are insufficient or do not support the EPA's claim that many existing sources will become ''modified'' sources in the future, while other existing sources will be replaced by new facilities or shut down.

Some commenters also assert that the compliance reports and the preliminary data submitted in response to the ICR indicate that the large majority of facilities in the oil and natural gas sector are not currently complying with the NSPS. This means, according to the commenters, that these sources are existing sources with limited turnover. One commenter adds that records of natural gas operations in New Mexico demonstrates that numerous oil and natural gas fugitive emissions sources, storage tanks, and loadout emissions sources with construction dates going back to 1970 have not been modified, reconstructed, or replaced with new equipment.

Market incentives. Many commenters generally agree with the EPA's statements in the 2019 Proposal that market incentives already provide a powerful impetus for owners and operators of sources in the oil and natural gas industry to limit their methane emissions. Commenters state that the fact that the ''pollutant'' at issue is itself a valuable commodity means that source owners and operators have economic incentives to prevent its release in order to maximize the amount of natural gas that is sold for revenue. One commenter notes that the EPA's data bear that out, demonstrating that over the past 80 years, the fraction of natural gas withdrawals lost to venting and flaring has decreased from over 20 percent to just 1 or 2 percent.

Conversely, other commenters contend that there are a number of flaws with the EPA's theory that market incentives will meaningfully address methane emissions from existing oil and natural gas sources. First, one commenter notes that these theoretical ''market incentives'' largely depend on natural gas price trajectories, and contends that the EPA fails to conduct any analysis of how operators might be anticipated to reduce their emissions in light of expected natural gas prices. In reality, the commenter states, examples abound of operators choosing to flare or vent gas, rather than capture it, under current market prices. Second, a commenter states that the EPA ignores a fundamental economic principle in its discussion of market incentives: When there is a negative externality associated with an activity (here, the emission of both climate-disrupting and conventional pollution) that is not reflected in an individual operator's costs, market incentives are typically insufficient to reduce the activity to socially optimal levels. Third, a commenter states that the emissions trends noted by the EPA do not support the proposition that market incentives are adequate to reduce methane emissions from existing sources; and in fact, the data cited by the EPA shows that emissions from the oil and natural gas industry have remained persistently high despite those incentives.

Voluntary actions. Several commenters present information regarding existing voluntary programs and methane mitigation strategies being employed to reduce methane emissions from oil and natural gas operations. These commenters present a series of voluntary programs/strategies that the industry is currently undertaking and will continue to undertake to help reduce its methane emissions.

One industry representative organization [American Petroleum Institute (API)] adds that participants in The Environmental Partnership's Leak Detection and Repair Program reported a leak occurrence rate of just 0.16 percent, and that figure comes from more than 156,000 surveys across more than 78,000 production sites and is an important signal that ongoing industry efforts to identify and fix emissions sources are working.

Several other commenters contend that voluntary measures to control methane emissions would not compensate for the removal of the Federal methane requirements. Commenters note that of the thousands of oil and natural gas sources across the U.S., only about 1 percent participate in voluntary programs to address methane emissions (citing *http://blogs.edf.org/energyexchange/2019/09/03/epas-proposal-to-rollback-methane-rules-ignores-scientific-evidence-will-lead-to-5-million-tons-of-methane-pollution/*).

Commenters note that even industry members that have participated in these voluntary programs have noted that they are not a substitute for strong, uniform regulatory requirements. In addition, some commenters state that while voluntary efforts are important for reducing emissions and understanding how production operations can become more efficient and deliver environmental benefits, they cannot replace uniform Federal methane regulations for the oil and natural gas industry.

State regulations. Some commenters agree with the EPA that there are several states—including many of the states with the most significant oil and natural gas activity levels, that are already taking actions to reduce VOC and, by extension, methane emissions. One commenter states that while not every state has adopted such regulations, the states the EPA cites in the proposal cover the vast majority of the nation's oil and natural gas production, and while not every state's regulatory program covers all of the emission sources listed in NSPS subparts OOOO and OOOOa, they do all include regulatory requirements for storage vessels and fugitive emissions at well sites, ''two of the largest emission sources within the oil and natural gas industry.'' Another commenter concludes that current regulations of VOC emissions in North Dakota and other top oil and natural gas producing states will be sufficient to reduce methane emissions from the oil and natural gas industry, and that the participation of those states in national organizations such as the Environmental Council of the States (ECOS) are generating increasingly consistent state requirements that will meaningfully reduce emissions should the proposed amendments be finalized.

Other commenters assert that emissions control requirements of state regulatory programs will not be sufficient to reduce methane emissions. Commenters note that California, Colorado, Montana, New Mexico, North Dakota, Ohio, Pennsylvania, Texas, Utah, and Wyoming—the states that the EPA includes in the Proposal's ''Comparison of State Oil and Natural Gas Regulations'' table, 84 FR 50277—take widely divergent approaches that vary significantly in stringency, and most states have no standards applicable to existing sources. In 2020, according to the commenters, state standards applicable to existing sources (certain standards in California, Colorado, Utah, Wyoming (in the Upper Green River Basin ozone non-attainment area), and Texas) will reduce only 180,000 metric tons of methane, roughly 5 percent of what CAA section 111(d) guidelines modeled on the current NSPS could achieve. Other commenters added that regulation of existing sources by the EPA under section 111(d) of the CAA is preferable to a patchwork of regulations created separately by each state Agency (or the lack of regulation in some states). One commenter explains that Federal regulation creates a consistent framework that establishes a minimum level of emission control that strengthens public confidence in the natural gas industry and ensures GHG emission reductions.

Modeling analyses of impacts of foregone regulation of existing sources. Commenters presented two competing modeling analyses estimating the potential impacts of not pursuing EGs under CAA section 111(d). One presented by API supported the EPA's statements in the 2019 Proposal that the impacts would be limited, and one presented by the Environmental Defense Fund (EDF) disputed the EPA's claim.[73] [74] The assumptions used in these analyses vary; including the assumed EG requirements, the date when emissions that could have and would be controlled under an EG, what sources/segments the EG would cover, and how they accounted for turnover rates and state regulations when projecting emissions from existing sources. Neither of these analyses provide sufficient detail by emission source by segment to do a direct comparison of their analyses. However, the most important driver of differences between the competing analyses appears to be the differing assumptions regarding the emissions sources and segments the EG would regulate and the date when emissions could have and would be controlled under an EG.

The API Analysis includes a subset of emission sources compared to the EDF Analysis. The API Analysis includes the following production sources: Storage vessels, pneumatic devices, pneumatic pumps, and fugitive emissions from non-low production wells—it does not include low production wells, reciprocating/centrifugal compressors, or fugitive emissions from gathering and boosting compressor stations based on what was covered under the 2016 *Control Techniques Guidelines for the Oil and Natural Gas Industry.*[75] The EDF Analysis assumes that the EG will extend the requirements found in the 2016 Rule to all affected existing sources, specifically: High-bleed pneumatic controllers at well sites and transmission and storage compressor stations, all continuous bleed pneumatic controllers at natural gas processing plants, fugitive emissions from gas processing plants, well sites, and compressor stations, reciprocating and centrifugal compressors at both processing plants and compressor stations, and pneumatic pumps at well sites and processing plants. The EDF Analysis estimates emissions uncontrolled from existing sources starting in 2017 that would have been controlled by an EG and API assumes that an EG would not have been implemented (and, therefore, uncontrolled emissions as a result of a lack of an EG would not apply) until 2028. In absence of any other assumptions, this difference leads to vastly different results.

According to the API Analysis, if an existing source rule were implemented in 2028, minimal methane emission reductions (5 percent − (102,000 MT (metric tons) methane) from NSPS regulated sources would be realized with their hypothetical reductions decaying to ~1 percent (24,000 MT) of the total emissions from regulated sources by 2043. The API Analysis concludes that by 2028, 94 percent (and by 2043, 99 percent) of oil and natural gas production will be regulated by 40 CFR part 60, subpart OOOO or OOOOa. In other words, the API Analysis estimates that an EG modeled after a modified version of the EPA's 2016 Control Techniques Guideline would only achieve an additional 5 percent of emissions reductions when compared to the NSPS regulations alone. The API provides that their analysis illustrates that an existing source rule would provide negligible environmental benefit.

This is in contrast to the EDF Analysis that estimates that each year that the EPA does not promulgate EG under CAA section 111(d) will allow substantial additional emissions. They estimate emissions that have occurred and will occur starting in 2017 through 2030 by the EPA's failure to adopt EGs, as well as the emission reductions possible if EGs were promulgated. For example, they estimate that, in 2021, 9.8

[73] Earth Systems Sciences, LLC (for API). Methane Emissions from Regulated Onshore Production Sources. Evaluating the Impact of Existing Federal and State Regulations. October 2019. (Docket ID Item No. EPA–HQ–OAR–2017–0757–2090, Appendix A) (API Analysis).

[74] EDF. Assessment of Harm to the Public from Foregoing Methane Guidelines for Existing Sources. November 21, 2019. (Docket ID Item No. EPA–HQ–OAR–2017–0757–2134; Appendix D) (EDF Analysis).

[75] U.S. EPA. Control Techniques Guidelines for the Oil and Natural Gas Industry. October 2016. EPA–453–/B–16–001). *https://www.epa.gov/sites/production/files/2016-10/documents/2016-ctg-oil-and-gas.pdf.*

million metric tons of methane will be emitted by affected existing sources. The EDF Analysis estimates that by 2030, emissions from existing sources will be substantial and have a cumulative impact of about 126 MMT of methane; about 29 MMT of VOC; and about 1.1 million tons of HAP. The EDF Analysis estimates that in the over 3 years since the EPA has promulgated the 2016 Rule, 33.4 MMT of methane have been emitted by existing oil and natural gas sources. They further estimate that 12.2 MMT of those methane emissions, or 37 percent, could have been avoided if EGs were in effect.

Response: The EPA's response to comments specific to the four factors cited by the EPA in the proposal preamble for why there would be limited impacts from not regulating existing oil and natural gas sources under CAA section 111(d), are provided in the following paragraphs. *Equipment turnover/source modifications.* For the first factor (equipment turnover/source modifications will result in existing sources being subject to the NSPS), the EPA reviewed information and analyses supporting the proposal's claim of a high turnover rate (limited impact of an EG) and information/analyses that supporting a low turnover rate (substantial impact of an EG).

Referring to the API and EDF Analyses, each of those analyses accounted for turnover and source modifications differently in their emissions projections in absence of an EG under CAA section 111(d). The approaches used and information provided in these analyses do not allow for a direct comparison on how their differing assumptions impact their results. The API Analysis does not include modification triggers in their projection modeling, contending that the lack of modification triggers in their model is a conservative assumption because it will underestimate the number of wells that are covered by NSPS requirements in the future. However, the API Analysis used historical well records to estimate a distribution for the expected lifetime of wells (and associated equipment) in each state. The EDF Analysis assumes that emissions attributable to existing sources decline year-over-year as existing sources are removed from operation or undertake modifications that subject them to regulation as modified sources under the 2016 Rule based on turnover rate percentages. Insufficient detail provided by EDF on where the turnover percentage rates they used in their analysis came from. It is unclear how the percentages used (existing source decline turnover rate of 5 percent for production sources, 4 percent for gathering and boosting sources, and 1 percent for all downstream sources) in the EDF Analysis were estimated.

The EPA recognizes the limitations pointed out by commenters regarding the GHGI (for pneumatic controllers, compressors, tank throughput, and well completions); *Drillinginfo.com* (for well completions); and NSPS subpart OOOOa compliance reports (for assessing turnover rates). As commenters indicate, when comparing activity counts, compliance reports, and preliminary information received in the ICR process, the data indicates that there is incomplete information to assess turnover and obsolescence rates. The justification of the EPA's rescission of the ICR is presented in a separate rulemaking action, ''Notice Regarding Withdrawal of Obligation To Submit Information'' (82 FR 12817, March 7, 2017). Absent further information (which is why we solicited comment on turnover rates) and time, where compliance report information can be assessed over a longer time period, there will continue to be a high level of uncertainty with any estimates on turnover/obsolescence rates.

The EPA maintains, however, as it did in the proposal, that equipment turnover and source modification are a factor (albeit difficult to quantify with any certainty) that will limit the emissions from existing sources in the oil and natural gas industry in the absence of a CAA section 111(d) EG. In addition to the reasons stated in the proposal, we acknowledge that it could take up to 7 to 10 years from date of promulgation of an EG for requirements to be fully implemented. During this time, the EPA expects that a percentage of existing sources will shut down or undertake modification, which will result in them becoming subject to regulation under CAA section 111(b). This turnover, in the case of well-sites, would likely be impacted as production declines and dependent on the economic viability of the well-site.

Lastly, the EPA acknowledges the information the state of New Mexico identifies that indicates that there are existing sources in that state that have never been modified as supporting that turnover and modifications will not be a factor that results in reducing emissions from oil and natural gas existing sources in that area in absence of an EG and accepts that these are examples of existing sources that have continued to operate for long periods of time without being reconstructed or modified.

Market incentives. With regards to the second factor (market incentives), as stated in section VII.B of this preamble, there are market incentives for the oil and natural gas industry to capture as much natural gas (and, by extension, methane) as is cost effective. Depending on the future trajectories of natural gas prices and the costs of natural gas capture and emission reductions, market incentives may continue to drive emission reductions, even in the absence of specific regulatory requirements applicable to methane emissions from existing sources. While it is a challenging concept to quantify in monetary terms, improving their environmental performance is increasingly important for firms to maintain a ''social license to operate.'' Generally speaking, the social license to operate means that the firm's employees, investors, customers, and the general public find that the firm's business activities and operations are acceptable to continue to freely participate in the marketplace. Maintaining the social license by improving environmental performance, such as reducing emissions, can help firms respond to the complex environment within which they operate in ways that are favorable to their longer-term business interests.

In response to the commenter that states that the emissions trends noted by the EPA do not support the proposition that market incentives are adequate to reduce methane emissions from existing sources in lieu of Federal regulation, the EPA is not making that claim. The EPA claims that market incentives are one factor (among others) that contribute and will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources in absence of an EG.

Voluntary action. With regards to the third factor (voluntary actions), the EPA maintains, and has received a lot of comments in support of, its position that the plethora of voluntary methane emissions mitigation programs will limit (among other factors) methane emissions increases from existing oil and natural gas industry emission sources in absence of a CAA section 111(d) EG. The EPA does acknowledge, however, as several commenters contend, that the industry as a whole is not uniformly meeting voluntary measures at the same level of control and that some companies may not be participating in cited voluntary methane emissions programs at all. This makes it difficult to verify the impacts on emissions as a result of voluntary program participation. Additional time will be needed to allow these programs to further develop and to be fully implemented to better quantify the impacts the varied programs have on limiting emissions from oil and natural gas industry sources.

In response to the commenters that contend that voluntary actions cannot be relied upon to reduce methane emissions from existing sources in lieu of Federal regulation, the EPA is not making that claim. As with other mitigating factors cited by the EPA, voluntary actions are one factor (among others) that contribute and will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources in absence of an EG.

State regulations. With regards to the fourth and final factor (state regulations), the EPA agrees that there could be an impact of not regulating existing oil and natural gas sources, but at this time, the EPA has not conducted a quantitative analysis of the impact of state regulatory programs to determine the degree to which those programs would reduce emissions from existing sources. The EPA also acknowledges that state requirements do vary in stringency and that only a subset of states include requirements for sources that the EPA could potentially define as existing sources. However, those states that have standards applicable to existing sources (certain standards in California, Colorado, Utah, Wyoming (in the Upper Green River Basin ozone non-attainment area), and Texas) account for a substantial portion of oil and natural gas production in the United States. The EPA also expects a percentage of existing sources to shut down or undertake modification which would make them become subject to certain state standards or permits. As one of the commenters points out, and the EPA agrees, while not every state has adopted specific methane emissions regulations for oil and natural gas industry existing sources, current regulations (and permits) controlling VOC emissions in North Dakota and other top oil and natural gas producing states will concurrently reduce methane emissions from the oil and natural gas industry.

In response to the commenters that contend that state regulations/permits that include oil and natural gas industry existing source emissions control requirements cannot be relied upon to reduce methane emissions from existing sources in lieu of Federal regulation, the EPA is not making that claim. As with other mitigating factors cited by the EPA, existing source state requirements are one factor (among others) that contribute and will continue to contribute to the downward trend of total methane emissions from oil and natural gas existing sources in absence of an EG.

XI. Impacts of This Final Rule

A. What are the air impacts?

The EPA projected that, from 2021 to 2030, relative to the baseline, the final rule will forgo about 448,000 short tons of methane emissions reductions (10.1 million tons CO_2 Eq.), 12,000 short tons of VOC emissions reductions, and 400 short tons of HAP emission reductions from facilities affected by this reconsideration.[76] The EPA estimated regulatory impacts beginning in 2021 as it is the first full year of implementation of this rule. The EPA estimated impacts through 2030 to illustrate the accumulating effects of this rule over a longer period. The EPA did not estimate impacts after 2030 for reasons including limited information, as explained in the RIA.

B. What are the energy impacts?

Energy impacts in this section are those energy requirements associated with the operation of emissions control devices. Potential impacts on the national energy economy from the rule are discussed in the economic impacts section. Under the final rule, there will likely be little change in the national energy demand resulting from the deregulatory actions finalized here.

C. What are the compliance costs?

The PV of the regulatory compliance cost reduction associated with this final rule over the 2021 to 2030 period was estimated to be $67 million (in 2016 dollars) using a 7-percent discount rate and $83 million using a 3-percent discount rate. The EAV of these cost reductions is estimated to be $8.9 million per year using a 7-percent discount rate and $9.4 million per year using a 3-percent discount rate.

These estimates do not, however, include the forgone producer revenues associated with the decrease in the recovery of saleable natural gas, though some of the compliance actions required in the baseline would likely have captured saleable product that would have otherwise been emitted to the atmosphere. Estimates of the value of the recovered product were included in previous regulatory analyses as offsetting compliance costs. Because of the deregulatory nature of this final action, the EPA projected a reduction in the recovery of saleable product. Using the 2020 Annual Energy Outlook (AEO) projection of natural gas prices to estimate the value of the change in the recovered gas at the wellhead projected to result from the final action, the EPA estimated a PV of regulatory compliance cost reductions of the final rule over the 2021 to 2030 period of $31 million using a 7-percent discount rate and $38 million using a 3-percent discount rate. The corresponding estimates of the EAV of cost reductions after accounting for the forgone revenues were $4.1 million per year using a 7-percent discount rate and $4.3 million per year using a 3-percent discount rate.

D. What are the economic and employment impacts?

The EPA used the National Energy Modeling System (NEMS) to estimate the impacts of the 2016 Rule on the U.S. energy system. The NEMS is a publicly available model of the U.S. energy economy developed and maintained by the EIA and is used to produce the AEO, a reference publication that provides detailed projections of the U.S. energy economy.[77] The EPA estimated small impacts on crude oil and natural gas markets of the 2016 Rule over the 2020 to 2025 period. This final rule will result in a decrease in total compliance costs relative to the baseline. Therefore, the EPA expects that this rule will partially reduce the impacts estimated for the 2016 Rule in the 2016 Rule RIA.

Executive Order 13563 directs Federal agencies to consider the effect of regulations on job creation and employment. According to the Executive order, ''our regulatory system must protect public health, welfare, safety, and our environment while promoting economic growth, innovation, competitiveness, and job creation. It must be based on the best available science.'' (Executive Order 13563, 2011). While a standalone analysis of employment impacts is not included in a standard benefit-cost analysis, such an analysis is of concern in the current economic climate given continued interest in the employment impact of regulations such as this proposed rule. The EPA estimated the change in compliance-related labor due to the reduced requirements for the installation, operation, and maintenance of control equipment, control activities, and labor associated with reporting and recordkeeping requirements in the 2016

[76] In a separate action, the EPA is finalizing technical reconsideration amendments to 40 CFR part 60, subpart OOOOa (EPA–HQ–OAR–2017–0483; FRL–10013–60–OAR; FR Doc. 2020–18115). These technical amendments were proposed in October 2018. 83 FR 52056. Please reference that final rule for the summary and rationale of those technical changes. Please refer to the RIA for both rules to see the combined impacts.

[77] *https://www.eia.gov/outlooks/aeo/.*

Rule RIA. Under the final rule, the EPA expects there will be slight reductions in the labor required for compliance-related activities associated with the 2016 Rule requirements relating to the rescission of requirements in the transmission and storage segment of the oil and natural gas industry.

E. What are the benefits of the final standards?

The EPA expects forgone climate and health benefits due to the forgone emissions reductions projected under this final rule. The EPA estimated the forgone domestic climate benefits from the forgone methane emissions reductions using an interim measure of the domestic social cost of methane (SC-CH_4). The SC-CH_4 estimates used here were developed under Executive Order 13783 for use in regulatory analyses until an improved estimate of the impacts of climate change to the U.S. can be developed based on the best available science and economics. Executive Order 13783 directed agencies to ensure that estimates of the social cost of GHG used in regulatory analyses ''are based on the best available science and economics'' and are consistent with the guidance contained in OMB Circular A–4, ''including with respect to the consideration of domestic versus international impacts and the consideration of appropriate discount rates'' (Executive Order 13783, Section 5(c)). In addition, Executive Order 13783 withdrew the technical support documents (TSDs) and the August 2016 Addendum to these TSDs describing the global social cost of GHG estimates developed under the prior Administration as no longer representative of government policy. The withdrawn TSDs and Addendum were developed by an interagency working group that included the EPA and other executive branch entities and were used in the 2016 Rule RIA.

The EPA estimated the PV of the forgone domestic climate benefits over the 2021 to 2030 period to be $17 million under a 7-percent discount rate and $63 million under a 3-percent discount rate. The EAV of these forgone benefits is estimated $2.2 million per year under a 7-percent discount rate and $7.2 million per year under a 3-percent discount rate. These values represent only a partial accounting of domestic climate impacts from methane emissions and do not account for health effects of ozone exposure from the increase in methane emissions.

Under the final rule, the EPA expects that forgone VOC emission reductions will degrade air quality and are likely to adversely affect health and welfare associated with exposure to ozone, $PM_{2.5}$, and HAP, but did not quantify these effects at this time. This omission should not imply that these forgone benefits may not exist; rather, it reflects the inherent difficulties in accurately modeling the direct and indirect impacts of the projected reductions in emissions for this industrial sector. To the extent that the EPA were to quantify these ozone and PM impacts, it would estimate the number and value of avoided premature deaths and illnesses using an approach detailed in the Particulate Matter NAAQS and Ozone NAAQS Regulatory Impact Analyses.[78 79] This approach relies on full-form air quality modeling. The Agency is committed to assessing ways of conducting full-form air quality modeling for the oil and natural gas sector that would be suitable for use in regulatory analysis in the context of NSPS, including ways to address the uncertainties regarding the scope and magnitude of VOC emissions.

When quantifying the incidence and economic value of the human health impacts of air quality changes, the Agency sometimes relies upon alternative approaches to using full-form air quality modeling, called reduced-form techniques, often reported as ''benefit-per-ton'' values that relate air pollution impacts to changes in air pollutant precursor emissions.[80] A small, but growing, literature characterizes the air quality and health impacts from the oil and natural gas sector.[81 82 83] The Agency feels more work needs to be done to vet the analysis and methodologies for all potential approaches for valuing the health effects of VOC emissions before they are used in regulatory analysis, but is committed to continuing this work. Recently, the EPA systematically compared the changes in benefits, and concentrations where available, from its benefit-per-ton technique and other reduced-form techniques against the changes in benefits and concentrations derived from full-form photochemical model representation of a few different specific emissions scenarios.[84] The Agency's goal was to create a methodology by which investigators could better understand the suitability of alternative reduced-form air quality modeling techniques for estimating the health impacts of criteria pollutant emissions changes in the EPA's benefit-cost analysis, including the extent to which reduced form models may over- or under-estimate benefits (compared to full-scale modeling) under different scenarios and air quality concentrations. The EPA Science Advisory Board (SAB) recently convened a panel to review this report.[85] In particular, the SAB will assess the techniques the Agency used to appraise these tools; the Agency's approach for depicting the results of reduced-form tools; and, steps the Agency might take for improving the reliability of reduced-form techniques for use in future Regulatory Impact Analyses RIAs. The scenario-specific emission inputs developed for this project are currently available online.[86] A thorough description of the study design and methodology is also available.[87]

XII. 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*.

[78] U.S. EPA. December 2012. Regulatory Impact Analysis for the Final Revisions to the National Ambient Air Quality Standards for Particulate Matter. EPA–452/R–12–005. Office of Air Quality Planning and Standards, Health and Environmental Impacts Division. *https://www3.epa.gov/ttnecas1/regdata/RIAs/finalria.pdf.* Accessed January 9, 2020.

[79] U.S. EPA. September 2015. Regulatory Impact Analysis of the Final Revisions to the National Ambient Air Quality Standards for Ground-Level Ozone. EPA–452/R–15–007. Office of Air Quality Planning and Standards, Health and Environmental Impacts Division. *https://www3.epa.gov/ttnecas1/docs/20151001ria.pdf.* Accessed January 9, 2020.

[80] U.S. EPA. February 2018. Technical Support Document: Estimating the Benefit per Ton of Reducing $PM_{2.5}$ Precursors from 17 Sectors. *https://www.epa.gov/sites/production/files/2018-02/documents/sourceapportionmentbpttsd_2018.pdf.* Accessed January 9, 2020.

[81] Fann, N., K.R. Baker, E.A.W. Chan, A. Eyth, A. Macpherson, E. Miller, and J. Snyder. 2018. ''Assessing Human Health $PM_{2.5}$ and Ozone Impacts from U.S. Oil and Natural Gas Sector Emissions in 2025.'' Environmental Science and Technology 52(15):8095–8103.

[82] Litovitz, A., A. Curtright, S. Abramzon, N. Burger, and C. Samaras. 2013. ''Estimation of Regional Air-Quality Damages from Marcellus Shale Natural Gas Extraction in Pennsylvania.'' Environmental Research Letters 8(1), 014017.

[83] Loomis, J. and M. Haefele. 2017. ''Quantifying Market and Non-market Benefits and Costs of Hydraulic Fracturing in the United States: A Summary of the Literature.'' Ecological Economics 138:160–167.

[84] This analysis compared the benefits estimated using full-form photochemical air quality modeling simulations (CMAQ and CAMx) against four reduced-form tools, including: InMAP; AP2/3; EASIUR; and EPA's benefit-per-ton.

[85] 85 FR 23823 (April 29, 2020).

[86] The scenario-specific emission inputs developed for this project and all associated documentation are currently available online at *https://github.com/epa-kpc/RFMEVAL.*

[87] Baker, K.R., M. Amend, S. Penn, J. Bankert, H. Simon, E. Chan, N. Fann, M. Zawacki, K. Davidson, K. and H. Roman. 2020. ''A Database for Evaluating the InMAP, APEEP, and EASIUR Reduced Complexity Air-Quality Modeling Tools.'' Data in Brief 28: 104886.

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

This action is a significant regulatory action that was submitted to the Office of Management and Budget (OMB) for review because it raises novel legal or policy issues. Any changes made in response to OMB recommendations have been documented in the docket. In addition, the EPA prepared an RIA of the potential costs and benefits associated with this final action. The RIA available in the docket describes in detail the empirical basis for the EPA's assumptions and characterizes the various sources of uncertainties affecting the estimates below. Table 8 shows the PV and EAV of the costs, benefits, and net benefits of the final rule for the 2021 to 2030 period relative to the baseline using discount rates of 7 and 3 percent, respectively. The table also shows the total forgone emission reductions projected from 2021 to 2030 relative to the baseline.

In the following table, we refer to the compliance cost reductions as the ''benefits'' and the forgone benefits as the ''costs'' of this final action. The net benefits are the benefits (total cost reductions) minus the costs (forgone domestic climate benefits).

TABLE 8—SUMMARY OF THE PV AND EAV OF THE MONETIZED FORGONE BENEFITS, COST REDUCTIONS, AND NET BENEFITS FROM 2021 TO 2030, 7- AND 3-PERCENT DISCOUNT RATES

[Millions of 2016$]

	7-Percent discount rate		3-Percent discount rate	
	PV	EAV	PV	EAV
Benefits (Total Cost Reductions)	$31	$4.1	$38	$4.3
Compliance Cost Reductions	*67*	*8.9*	*83*	*9.4*
Forgone Value of Product Recovery	*36*	*4.7*	*45*	*5.1*
Costs (Forgone Domestic Climate Benefits)	17	2.2	63	7.2
Net Benefits	14	1.9	−25	−2.9
Non-Monetized Forgone Benefits	Non-monetized climate impacts from increases in methane emissions. Health effects of $PM_{2.5}$ and ozone exposure from an increase of about 11,000 short tons of VOC from 2021 through 2030. Health effects of HAP exposure from an increase of about 330 short tons of HAP from 2021 through 2030. Health effects of ozone exposure from an increase of about 400,000 short tons of methane from 2021 through 2030. Visibility impairment. Vegetation effects.			

Note: Estimates may not sum due to independent rounding.

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

This action is considered an Executive Order 13771 deregulatory action. Details on the estimated cost savings of this final rule can be found in the EPA's analysis of the potential costs and benefits associated with this action.

C. Paperwork Reduction Act (PRA)

The information collection activities in this final rule have been submitted for approval to OMB under the PRA. The ICR document that the EPA prepared has been assigned EPA ICR number 2604.02 and OMB Control Number 2060–0729. The information collection requirements are not enforceable until OMB approves them.

A summary of the information collection activities previously submitted to the OMB for the final action titled ''Standards of Performance for Crude Oil and Natural Gas Facilities for Construction, Modification, or Reconstruction'' (2016 Rule) under the PRA, and assigned OMB Control Number 2060–0721 (EPA ICR number 2523.02), can be found at 81 FR 35890. You can find a copy of the ICR in the 2016 Rule Docket (Docket ID Item No. EPA–HQ–OAR–2010–0505–7626). In this rule, the EPA is finalizing the information collection activities as a result of the EPA's review under Executive Order 13783 (EPA ICR number 2604.02). These final changes (2020 NSPS Subpart OOOOa Executive Order 13783 Review Final) would remove reporting and recordkeeping requirements associated with the rescinded requirements.[88]

Comments were received on the October 15, 2018 (83 FR 52056) proposed rule indicating that the recordkeeping and reporting burden for the 2016 Rule was significantly underestimated. In particular, the commenters pointed to the estimated burden associated with the fugitive emissions requirements. As a result of these comments, the EPA reexamined the analysis for the 2016 Rule recordkeeping and reporting burden and made adjustments where warranted. This resulted in an updated and more accurate assessment of the recordkeeping and reporting burden for the 2016 Rule. The updated 2016 Rule recordkeeping and reporting burden was estimated at a 3-year annual average of 689,154 hours and $110,336,343 (2016$) over the 3-year period. These figures represent the ''baseline'' from which changes made in these final amendments (2020 NSPS Subpart OOOOa Executive Order 13783 Review Final) can be compared. Burden associated with this rule (2020 Rule E.O. 13783 Review Final):

Respondents/affected entities: Oil and natural gas operators and owners.

Respondent's obligation to respond: Mandatory.

Estimated number of respondents: 519.

[88] In a separate action, the EPA is finalizing technical reconsideration amendments to NSPS subpart OOOOa (EPA–HQ–OAR–2017–0483; FRL–10013–60–OAR; FR Doc. 2020–18115). These technical amendments where proposed in October 2018. 83 FR 52056. The information collection burden for the combination of these NSPS subpart OOOOa Reconsideration final amendments and the Policy Review final amendments is addressed in a separate ICR (OMB Control Number 2060–0721; EPA ICR number 2523.04).

Frequency of response: Varies depending on affected facility.[89]

Total estimated burden: 680,841 hours (per year). Burden is defined at 5 CFR 1320.3(b).

Total estimated cost: $108,723,359 (2016$), which includes no capital or O&M costs.

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. The OMB control numbers for the EPA's regulations in 40 CFR are listed in 40 CFR part 9. When OMB approves this ICR, the Agency will announce that approval in the **Federal Register** and publish a technical amendment to 40 CFR part 9 to display the OMB control number for the approved information collection activities contained in this final rule.

D. Regulatory Flexibility Act (RFA)

I certify that this action will not have a significant economic impact on a substantial number of small entities under the RFA. In making this determination, the impact of concern is any significant adverse economic impact on small entities. An agency may certify that a rule will not have a significant economic impact on a substantial number of small entities if the rule relieves regulatory burden, has no net burden, or otherwise has a positive economic effect on the small entities subject to the rule. This is a deregulatory action, and the burden on all entities affected by this final rule, including small entities, is the same or reduced compared to the 2016 Rule. *See* the discussion in section XI of this preamble and the RIA for details. The EPA has, therefore, concluded that this action will have no net increase regulatory burden for all directly regulated small entities.

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. The action imposes no enforceable duty on any state, local, or tribal governments or the private sector.

F. Executive Order 13132: Federalism

This action does not have federalism implications. It will 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.

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

This action does not have tribal implications as specified in Executive Order 13175. It will not have substantial direct effects 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, as specified in Executive Order 13175. Thus, Executive Order 13175 does not apply to this action.

Consistent with the EPA Policy on Consultation and Coordination with Indian Tribes, on September 10, 2019, the EPA sent a letter to all tribal governments inviting consultation. Additionally, on August 29, 2019, and September 18, 2019, the EPA provided an overview of the proposed rule to the National Tribal Air Association. The EPA did not receive any requests for consultation.

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

This action is not subject to Executive Order 13045 because it is not economically significant as defined in Executive Order 12866. The 2016 Rule, as discussed in the RIA,[90] was anticipated to reduce emissions of methane, VOC, and HAP, and some of the benefits of reducing these pollutants would have accrued to children. The final rule is expected to decrease the impact of the emissions reductions estimated from the 2016 Rule on these benefits, as discussed in the RIA.

The final action does not affect the level of public health and environmental protection already being provided by existing NAAQS and other mechanisms in the CAA. This final action does not affect applicable local, state, or Federal permitting or air quality management programs that will continue to address areas with degraded air quality and maintain the air quality in areas meeting current standards. Areas that need to reduce criteria air pollution to meet the NAAQS will still need to rely on control strategies to reduce emissions. The EPA does not believe the decrease in emission reductions projected by the final rule will have a disproportionate adverse effect on children's health.

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

This action is not a ''significant energy action'' because it is not likely to have a significant adverse effect on the supply, distribution, or use of energy. In the RIA accompanying the 2016 Rule, the EPA used the NEMS to estimate the impacts of the 2016 Rule on the United States energy system. The EPA estimated small impacts of that rule over the 2020 to 2025 period relative to the baseline for that rule. This final rule is estimated to result in a decrease in total compliance costs, with the reduction in costs affecting a subset of the affected entities under NSPS subpart OOOOa. Therefore, the EPA expects that this deregulatory action will reduce the impacts estimated for the final NSPS in the 2016 RIA and, as such, is not a significant energy action.

J. National Technology Transfer and Advancement Act (NTTAA)

This 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 final action is unlikely to have disproportionately high and adverse human health or environmental effects on minority populations, low-income populations, and/or indigenous peoples, as specified in Executive Order 12898 (59 FR 7629, February 16, 1994). The 2016 Rule was anticipated to reduce emissions of methane, VOC, and HAP, and some of the benefits of reducing these pollutants would have accrued to minority populations, low-income populations, and/or indigenous peoples. The final rule is expected to decrease the impact of the emission reductions estimated from the 2016 Rule on these benefits. These communities may experience forgone benefits as a result of this action, as discussed in the RIA.

This final action does not affect the level of public health and environmental protection already being provided by existing NAAQS and other mechanisms in the CAA. This final action does not affect applicable local, state, or Federal permitting or air quality management programs that will continue to address areas with degraded air quality and maintain the air quality in areas meeting current standards. Areas that need to reduce criteria air pollution to meet the NAAQS will still

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[89] The specific frequency for each information collection activity within this request is shown in Tables 1a through 1d of the Supporting Statement in the public docket.

[90] *See* Final RIA in the public docket for this rulemaking.

need to rely on control strategies to reduce emissions.

The EPA believes that this final action is unlikely to have disproportionately high and adverse human health or environmental effects on minority populations, low-income populations, and/or indigenous peoples. The EPA notes that the potential impacts of the final rule are not expected to be experienced uniformly, and the distribution of avoided compliance costs associated with this action depends on the degree to which costs would have been passed through to consumers.

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. This action is not a ''major rule'' as defined by 5 U.S.C. 804(2).

List of Subjects in 40 CFR Part 60

Environmental protection, Administrative practice and procedure, Air pollution control, Reporting and recordkeeping requirements.

Andrew Wheeler,

Administrator.

For the reasons set forth in the preamble, the EPA amends 40 CFR part 60 as follows:

PART 60—STANDARDS OF PERFORMANCE FOR NEW STATIONARY SOURCES

■ 1. The authority citation for part 60 continues to read as follows:

Authority: 42 U.S.C. 7401 *et seq.*

■ 2. Revise the heading of subpart OOOO to read as follows:

Subpart OOOO—Standards of Performance for Crude Oil and Natural Gas Facilities for Which Construction, Modification, or Reconstruction Commenced After August 23, 2011, and on or Before September 18, 2015

■ 3. Section 60.5360 is amended to read as follows:

§ 60.5360 What is the purpose of this subpart?

This subpart establishes emission standards and compliance schedules for the control of volatile organic compounds (VOC) and sulfur dioxide (SO_2) emissions from affected facilities in the crude oil and natural gas production source category that commence construction, modification, or reconstruction after August 23, 2011, and on or before September 18, 2015.

■ 4. Section 60.5365 is amended by revising the introductory text and paragraphs (b), (c), and (d)(1), removing and reserving paragraph (d)(2), and revising paragraph (e) introductory text to read as follows:

§ 60.5365 Am I subject to this subpart?

You are subject to the applicable provisions of this subpart if you are the owner or operator of one or more of the onshore affected facilities listed in paragraphs (a) through (g) of this section that is located within the Crude Oil and Natural Gas Production source category, as defined in § 60.5430 for which you commence construction, modification, or reconstruction after August 23, 2011, and on or before September 18, 2015.

* * * * *

(b) Each centrifugal compressor affected facility, which is a single centrifugal compressor using wet seals. A centrifugal compressor located at a well site, or an adjacent well site and servicing more than one well site, is not an affected facility under this subpart.

(c) Each reciprocating compressor affected facility, which is a single reciprocating compressor. A reciprocating compressor located at a well site, or an adjacent well site and servicing more than one well site, is not an affected facility under this subpart.

(d)(1) For the oil and natural gas production segment, each pneumatic controller affected facility, which is a single continuous bleed natural gas-driven pneumatic controller operating at a natural gas bleed rate greater than 6 standard cubic feet per hour.

* * * * *

(e) Each storage vessel affected facility, which is a single storage vessel, and has the potential for VOC emissions equal to or greater than 6 tons per year (tpy) as determined according to this section by October 15, 2013, for Group 1 storage vessels and by April 15, 2014, or 30 days after startup (whichever is later) for Group 2 storage vessels, except as provided in paragraphs (e)(1) through (4) of this section. The potential for VOC emissions must be calculated using a generally accepted model or calculation methodology, based on the maximum average daily throughput determined for a 30-day period of production prior to the applicable emission determination deadline specified in this section. The determination may take into account requirements under a legally and practically enforceable limit in an operating permit or other requirement established under a Federal, State, local or tribal authority.

* * * * *

■ 5. Section 60.5420 is amended by revising paragraph (c)(5)(iv) to read as follows:

§ 60.5420 What are my notification, reporting, and recordkeeping requirements?

* * * * *

(c) * * *

(5) * * *

(iv) For storage vessels that are skid-mounted or permanently attached to something that is mobile (such as trucks, railcars, barges, or ships), records indicating the number of consecutive days that the vessel is located at the site. If a storage vessel is removed from the site and, within 30 days, is either returned to or replaced by another storage vessel at the site to serve the same or similar function, then the entire period since the original storage vessel was first located at the site, including the days when the storage vessel was removed, will be added to the count towards the number of consecutive days.

* * * * *

■ 6. Section 60.5430 is amended by:

■ a. Adding the definition for *Crude Oil and Natural Gas Production source category* in alphabetical order.

■ b. Revising the definition of *Custody transfer.*

■ c. Adding the definitions for *Local distribution company (LDC) custody transfer station* and *Natural gas transmission and storage segment* in alphabetical order.

The additions and revision read as follows:

§ 60.5430 What definitions apply to this subpart?

* * * * *

Crude Oil and Natural Gas Production source category means:

(1) Crude oil production, which includes the well and extends to the point of custody transfer to the crude oil transmission pipeline or any other forms of transportation; and

(2) Natural gas production and processing, which includes the well and extends to, but does not include, the point of custody transfer to the natural gas transmission and storage segment.

Custody transfer means the transfer of crude oil or natural gas after processing and/or treatment in the producing operations, or from storage vessels or automatic transfer facilities or other such equipment, including product loading racks, to pipelines or any other forms of transportation.

* * * * *

Local distribution company (LDC) custody transfer station means a metering station where the LDC receives a natural gas supply from an upstream supplier, which may be an interstate transmission pipeline or a local natural gas producer, for delivery to customers through the LDC's intrastate transmission or distribution lines.

* * * * *

Natural gas transmission and storage segment means the transport or storage of natural gas prior to delivery to a ''local distribution company custody transfer station'' (as defined in this section) or to a final end user (if there is no local distribution company custody transfer station). For the purposes of this subpart, natural gas enters the natural gas transmission and storage segment after the natural gas processing plant, when present. If no natural gas processing plant is present, natural gas enters the natural gas transmission and storage segment after the point of ''custody transfer'' (as defined in this section). A compressor station that transports natural gas prior to the point of ''custody transfer'' or to a natural gas processing plant (if present) is not considered a part of the natural gas transmission and storage segment.

* * * * *

Subpart OOOOa—Standards of Performance for Crude Oil and Natural Gas Facilities for Which Construction, Modification, or Reconstruction Commenced After September 18, 2015

■ 7. Section 60.5360a is revised to read as follows:

§ 60.5360a What is the purpose of this subpart?

(a) This subpart establishes emission standards and compliance schedules for the control of volatile organic compounds (VOC) and sulfur dioxide (SO_2) emissions from affected facilities in the Crude Oil and Natural Gas Production source category that commence construction, modification, or reconstruction after September 18, 2015. The effective date of the rule in this subpart is August 2, 2016.

(b) [Reserved]

■ 8. Section 60.5365a is amended by revising the introductory text to read as follows:

§ 60.5365a Am I subject to this subpart?

You are subject to the applicable provisions of this subpart if you are the owner or operator of one or more of the onshore affected facilities listed in paragraphs (a) through (j) of this section, that is located within the Crude Oil and Natural Gas Production source category, as defined in § 60.5430a, for which you commence construction, modification, or reconstruction after September 18, 2015.

* * * * *

■ 9. Section 60.5375a is amended by revising the section heading and introductory text to read as follows:

§ 60.5375a What VOC standards apply to well affected facilities?

If you are the owner or operator of a well affected facility as described in § 60.5365a(a) that also meets the criteria for a well affected facility in § 60.5365(a) (in subpart OOOO of this part), you must reduce VOC emissions by complying with paragraphs (a) through (g) of this section. If you own or operate a well affected facility as described in § 60.5365a(a) that does not meet the criteria for a well affected facility in § 60.5365(a) (in subpart OOOO of this part), you must reduce VOC emissions by complying with paragraphs (f)(3) and (4) or paragraph (g) of this section for each well completion operation with hydraulic fracturing prior to November 30, 2016, and you must comply with paragraphs (a) through (g) of this section for each well completion operation with hydraulic fracturing on or after November 30, 2016.

* * * * *

■ 10. Section 60.5380a is amended by revising the section heading, introductory text, and paragraph (a)(1) to read as follows:

§ 60.5380a What VOC standards apply to centrifugal compressor affected facilities?

You must comply with the VOC standards in paragraphs (a) through (d) of this section for each centrifugal compressor affected facility.

(a)(1) You must reduce VOC emissions from each centrifugal compressor wet seal fluid degassing system by 95.0 percent.

* * * * *

■ 11. Section 60.5385a is amended by revising the section heading, introductory text, and paragraph (a)(3) to read as follows:

§ 60.5385a What VOC standards apply to reciprocating compressor affected facilities?

You must reduce VOC emissions by complying with the standards in paragraphs (a) through (d) of this section for each reciprocating compressor affected facility.

(a) * * *

(3) Collect the VOC emissions from the rod packing using a rod packing emissions collection system that operates under negative pressure and route the rod packing emissions to a process through a closed vent system that meets the requirements of § 60.5411a(a) and (d).

* * * * *

■ 12. Section 60.5390a is amended by revising the section heading and introductory text to read as follows:

§ 60.5390a What VOC standards apply to pneumatic controller affected facilities?

For each pneumatic controller affected facility you must comply with the VOC standards, based on natural gas as a surrogate for VOC, in either paragraph (b)(1) or (c)(1) of this section, as applicable. Pneumatic controllers meeting the conditions in paragraph (a) of this section are exempt from the requirements in paragraph (b)(1) or (c)(1) of this section.

* * * * *

■ 13. Section 60.5393a is amended by revising the section heading and introductory text to read as follows:

§ 60.5393a What VOC standards apply to pneumatic pump affected facilities?

For each pneumatic pump affected facility you must comply with the VOC standards, based on natural gas as a surrogate for VOC, in either paragraph (a) or (b) of this section, as applicable, on or after November 30, 2016.

* * * * *

■ 14. Section 60.5397a is amended by revising the section heading and introductory text to read as follows:

§ 60.5397a What fugitive emissions VOC standards apply to the affected facility which is the collection of fugitive emissions components at a well site and the affected facility which is the collection of fugitive emissions components at a compressor station?

For each affected facility under § 60.5365a(i) and (j), you must reduce VOC emissions by complying with the requirements of paragraphs (a) through (j) of this section. The requirements in this section are independent of the closed vent system and cover requirements in § 60.5411a.

* * * * *

■ 15. Section 60.5398a is amended by revising the section heading and paragraphs (a) and (d)(1)(xi) to read as follows:

§ 60.5398a What are the alternative means of emission limitations for VOC from well completions, reciprocating compressors, the collection of fugitive emissions components at a well site and the collection of fugitive emissions components at a compressor station?

(a) If, in the Administrator's judgment, an alternative means of emission limitation will achieve a reduction in VOC emissions at least equivalent to the reduction in VOC emissions achieved under §§ 60.5375a, 60.5385a, and 60.5397a, the Administrator will publish, in the **Federal Register**, a notice permitting the use of that alternative means for the purpose of compliance with §§ 60.5375a, 60.5385a, and 60.5397a. The notice may condition permission on requirements related to the operation and maintenance of the alternative means.

* * * * *

(d) * * *

(1) * * *

(xi) Operation and maintenance procedures and other provisions necessary to ensure reduction in VOC emissions at least equivalent to the reduction in VOC emissions achieved under § 60.5397a.

* * * * *

■ 16. Section 60.5400a is amended by revising the section heading and paragraph (c) to read as follows:

§ 60.5400a What equipment leak VOC standards apply to affected facilities at an onshore natural gas processing plant?

* * * * *

(c) You may apply to the Administrator for permission to use an alternative means of emission limitation that achieves a reduction in emissions of VOC at least equivalent to that achieved by the controls required in this subpart according to the requirements of § 60.5402a.

* * * * *

■ 17. Section 60.5401a is amended by revising the section heading to read as follows:

§ 60.5401a What are the exceptions to the equipment leak VOC standards for affected facilities at onshore natural gas processing plants?

* * * * *

■ 18. Section 60.5402a is amended by revising the section heading and paragraphs (a) and (d)(2) introductory text to read as follows:

§ 60.5402a What are the alternative means of emission limitations for VOC equipment leaks from onshore natural gas processing plants?

(a) If, in the Administrator's judgment, an alternative means of emission limitation will achieve a reduction in VOC emissions at least equivalent to the reduction in VOC emissions achieved under any design, equipment, work practice or operational standard, the Administrator will publish, in the **Federal Register**, a notice permitting the use of that alternative means for the purpose of compliance with that standard. The notice may condition permission on requirements related to the operation and maintenance of the alternative means.

* * * * *

(d) * * *

(2) The application must include operation, maintenance, and other provisions necessary to assure reduction in VOC emissions at least equivalent to the reduction in VOC emissions achieved under the design, equipment, work practice or operational standard in paragraph (a) of this section by including the information specified in paragraphs (d)(2)(i) through (x) of this section.

* * * * *

■ 19. Section 60.5410a is amended by revising paragraphs (a) introductory text, (b)(1), (d) introductory text, and (f) to read as follows:

§ 60.5410a How do I demonstrate initial compliance with the standards for my well, centrifugal compressor, reciprocating compressor, pneumatic controller, pneumatic pump, storage vessel, collection of fugitive emissions components at a well site, collection of fugitive emissions components at a compressor station, and equipment leaks and sweetening unit affected facilities at onshore natural gas processing plants?

* * * * *

(a) To achieve initial compliance with the VOC standards for each well completion operation conducted at your well affected facility you must comply with paragraphs (a)(1) through (4) of this section.

* * * * *

(b)(1) To achieve initial compliance with standards for your centrifugal compressor affected facility you must reduce VOC emissions from each centrifugal compressor wet seal fluid degassing system by 95.0 percent or greater as required by § 60.5380a(a) and as demonstrated by the requirements of § 60.5413a.

* * * * *

(d) To achieve initial compliance with VOC emission standards for your pneumatic controller affected facility you must comply with the requirements specified in paragraphs (d)(1) through (6) of this section, as applicable.

* * * * *

(f) For affected facilities at onshore natural gas processing plants, initial compliance with the VOC standards is demonstrated if you are in compliance with the requirements of § 60.5400a.

* * * * *

■ 20. Section 60.5412a is amended by paragraphs (a)(1)(i) and (a)(2) to read as follows:

§ 60.5412a What additional requirements must I meet for determining initial compliance with control devices used to comply with the emission standards for my centrifugal compressor, and storage vessel affected facilities?

* * * * *

(a) * * *

(1) * * *

(i) You must reduce the mass content of VOC in the gases vented to the device by 95.0 percent by weight or greater as determined in accordance with the requirements of § 60.5413a(b), with the exceptions noted in § 60.5413a(a).

* * * * *

(2) Each vapor recovery device (*e.g.,* carbon adsorption system or condenser) or other non-destructive control device must be designed and operated to reduce the mass content of VOC in the gases vented to the device by 95.0 percent by weight or greater as determined in accordance with the requirements of § 60.5413a(b). As an alternative to the performance testing requirements in § 60.5413a(b), you may demonstrate initial compliance by conducting a design analysis for vapor recovery devices according to the requirements of § 60.5413a(c).

* * * * *

■ 21. Section 60.5413a is amended by revising paragraph (d)(11)(iii) to read as follows:

§ 60.5413a What are the performance testing procedures for control devices used to demonstrate compliance at my centrifugal compressor and storage vessel affected facilities?

* * * * *

(d) * * *

(11) * * *

(iii) A manufacturer must demonstrate a destruction efficiency of at least 95 percent for THC, as propane. A control device model that demonstrates a destruction efficiency of 95 percent for THC, as propane, will meet the control requirement for 95-percent destruction of VOC (if applicable) required under this subpart.

* * * * *

■ 22. Section 60.5415a is amended by revising paragraphs (b)(1) and (f) to read as follows:

§ 60.5415a How do I demonstrate continuous compliance with the standards for my well, centrifugal compressor, reciprocating compressor, pneumatic controller, pneumatic pump, storage vessel, collection of fugitive emissions components at a well site, and collection of fugitive emissions components at a compressor station affected facilities, and affected facilities at onshore natural gas processing plants?

* * * * *

(b) * * *

(1) You must reduce VOC emissions from the wet seal fluid degassing system by 95.0 percent or greater.

* * * * *

(f) For affected facilities at onshore natural gas processing plants, continuous compliance with VOC requirements is demonstrated if you are in compliance with the requirements of § 60.5400a.

* * * * *

■ 23. Section 60.5420a is amended by revising paragraph (c)(5)(iv) to read as follows:

§ 60.5420a What are my notification, reporting, and recordkeeping requirements?

* * * * *

(c) * * *

(5) * * *

(iv) For storage vessels that are skid-mounted or permanently attached to something that is mobile (such as trucks, railcars, barges, or ships), records indicating the number of consecutive days that the vessel is located at a site in the Crude Oil and Natural Gas source category. If a storage vessel is removed from a site and, within 30 days, is either returned to the site or replaced by another storage vessel at the site to serve the same or similar function, then the entire period since the original storage vessel was first located at the site, including the days when the storage vessel was removed, will be added to the count towards the number of consecutive days.

* * * * *

■ 24. Section 60.5421a is amended by revising the section heading to read as follows:

§ 60.5421a What are my additional recordkeeping requirements for my affected facility subject to VOC requirements for onshore natural gas processing plants?

* * * * *

■ 25. Section 60.5422a is amended by revising the section heading to read as follows:

§ 60.5422a What are my additional reporting requirements for my affected facility subject to VOC requirements for onshore natural gas processing plants?

* * * * *

■ 26. Section 60.5430a is amended by:

■ a. Revising the definition for *Compressor station.*

■ b. Removing the definition for *Crude oil and natural gas source category.*

■ c. Adding the definition for *Crude Oil and Natural Gas Production source category* in alphabetical order.

■ d. Revising the definitions for *Equipment* and *Fugitive emissions component.*

■ e. Adding the definition for *Natural gas transmission and storage segment* in alphabetical order.

The revisions and additions read as follows:

§ 60.5430a What definitions apply to this subpart?

* * * * *

Compressor station means any permanent combination of one or more compressors that move natural gas at increased pressure through gathering pipelines. This includes, but is not limited to, gathering and boosting stations. The combination of one or more compressors located at a well site, or located at an onshore natural gas processing plant, is not a compressor station for purposes of § 60.5397a.

* * * * *

Crude Oil and Natural Gas Production source category means:

(1) Crude oil production, which includes the well and extends to the point of custody transfer to the crude oil transmission pipeline or any other forms of transportation; and

(2) Natural gas production and processing, which includes the well and extends to, but does not include, the point of custody transfer to the natural gas transmission and storage segment.

* * * * *

Equipment, as used in the standards and requirements in this subpart relative to the equipment leaks of VOC from onshore natural gas processing plants, means each pump, pressure relief device, open-ended valve or line, valve, and flange or other connector that is in VOC service or in wet gas service, and any device or system required by those same standards and requirements in this subpart.

* * * * *

Fugitive emissions component means any component that has the potential to emit fugitive emissions of VOC at a well site or compressor station, including valves, connectors, pressure relief devices, open-ended lines, flanges, covers, and closed vent systems not subject to § 60.5411 or § 60.5411a, thief hatches or other openings on a controlled storage vessel not subject to § 60.5395 or § 60.5395a, compressors, instruments, and meters. Devices that vent as part of normal operations, such as natural gas-driven pneumatic controllers or natural gas-driven pumps, are not fugitive emissions components, insofar as the natural gas discharged from the device's vent is not considered a fugitive emission. Emissions originating from other than the device's vent, such as the thief hatch on a controlled storage vessel, would be considered fugitive emissions.

* * * * *

Natural gas transmission and storage segment means the transport or storage of natural gas prior to delivery to a ''local distribution company custody transfer station'' (as defined in this section) or to a final end user (if there is no local distribution company custody transfer station). For the purposes of this subpart, natural gas enters the natural gas transmission and storage segment after the natural gas processing plant, when present. If no natural gas processing plant is present, natural gas enters the natural gas transmission and storage segment after the point of ''custody transfer'' (as defined in this section). A compressor station that transports natural gas prior to the point of ''custody transfer'' or to a natural gas processing plant (if present) is not considered a part of the natural gas transmission and storage segment.

* * * * *

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FEDERAL REGISTER

Vol. 85 No. 178

Monday, September 14, 2020

Part V

The President

Presidential Determination No. 2020–10 of September 9, 2020—Continuation of the Exercise of Certain Authorities Under the Trading With the Enemy Act

Federal Register
Vol. 85, No. 178
Monday, September 14, 2020

Presidential Documents

Title 3—

The President

Presidential Determination No. 2020–10 of September 9, 2020

Continuation of the Exercise of Certain Authorities Under the Trading With the Enemy Act

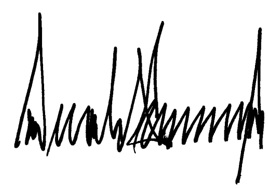
Memorandum for the Secretary of State [and] the Secretary of the Treasury

Under section 101(b) of Public Law 95–223 (91 Stat. 1625; 50 U.S.C. 4305 note), and a previous determination on September 13, 2019 (84 *FR* 49189, September 18, 2019), the exercise of certain authorities under the Trading With the Enemy Act is scheduled to expire on September 14, 2020.

I hereby determine that the continuation of the exercise of those authorities with respect to Cuba for 1 year is in the national interest of the United States.

Therefore, consistent with the authority vested in me by section 101(b) of Public Law 95–223, I continue for 1 year, until September 14, 2021, the exercise of those authorities with respect to Cuba, as implemented by the Cuban Assets Control Regulations, 31 CFR part 515.

The Secretary of the Treasury is authorized and directed to publish this determination in the *Federal Register*.



THE WHITE HOUSE,
Washington, September 9, 2020

[FR Doc. 2020–20377
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