controlled foreign corporation in that separate category.

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Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Approved: December 13, 2000.

Jonathan Talisman,

Acting Assistant Secretary (Tax Policy).

[FR Doc. 00–32477 Filed 12–29–00; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[TD 8914]

RIN 1545–AX67

Definition of Hyperinflationary Currency for Purposes of Section 988

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations concerning when a currency will be considered hyperinflationary for purposes of section 988. These final regulations are intended to prevent distortions associated with the computation of income and expense arising from section 988 transactions denominated in hyperinflationary currencies.

DATES: The effective date of this regulation is February 14, 2000.

FOR FURTHER INFORMATION CONTACT: John W. Rogers III of the Office of Associate Chief Counsel (International) at (202) 622–3870.

SUPPLEMENTARY INFORMATION:

Background

This document contains final Income Tax Regulations (26 CFR part 1) under section 988 of the Internal Revenue Code (Code). On March 17, 1992, the IRS and Treasury published final regulations (57 FR 9172) relating to the taxation of section 988 transactions, including, inter alia, transactions denominated in hyperinflationary currencies. Also on March 17, 1992, proposed regulations were published (57 FR 9217) relating to the treatment of certain financial instruments denominated in hyperinflationary currencies. The proposed regulations did not separately define hyperinflationary currency. Rather, they simply made reference to the definition in the final regulations, § 1.988–1(f).

TD 8860 (65 FR 2026) (January 13, 2000) finalized the proposed regulations relating to the treatment of financial instruments denominated in hyperinflationary currencies. Also in that issue of the **Federal Register** was a notice of proposed rulemaking regarding a proposed change in the period of years that are considered in determining whether a currency is hyperinflationary for purposes of section 988 (base period). The notice of proposed rulemaking also provided notice of a public hearing on the proposed regulations. No requests to speak were received, and the public hearing was canceled. This Treasury decision finalizes the proposed regulations relating to the change in base period, with certain minor changes.

Explanation of Provisions

As set out in the notice of proposed rulemaking, the term hyperinflationary currency, as defined in § 1.988–1(f), utilizes the definition in § 1.985–1(b)(2)(ii)(D). This definition was developed in the context of the Dollar Approximate Separate Transactions Method (DASTM) regulations, § 1.985–3, and generally considers the cumulative effects of inflation over the base period in determining whether a currency is hyperinflationary. In § 1.985–1(b)(2)(ii)(D), the base period consists of the thirty-six calendar month period immediately preceding the first day of the current calendar year. Use of this base period is generally appropriate in the context of DASTM because a qualified business unit needs to know in advance if it is subject to § 1.985–3 calculations.

However, failure to take the current year's inflation into account for purposes of computing foreign currency gain or loss under section 988 may lead to distortions in income and expense because inflation may rise dramatically in single year. Accordingly, the IRS and Treasury believe that for purposes of section 988, it is more appropriate to consider the cumulative inflation rate over the thirty-six month period ending on the last day of the taxpayer's (or the qualified business unit's) current taxable year. This change in the base period, however, applies only for the purposes of section 988 and not for the purpose of determining whether a taxpayer (or QBU) is subject to the provisions of § 1.985–3.

Summary of Comments

One comment was received in connection with the proposed change in the measurement of the base period under section 988. This comment relates to the application of the rule to regulated investment companies (RICs). The commenter stated that sections 852(a) and 4982 effectively require a RIC to distribute essentially all of its income during the calendar year in which it is earned. Thus, the commenter concluded that RICs need to know before the end of their tax year whether a particular currency is hyperinflationary. The Treasury and IRS recognize that the revised definition of base period could present an administrative burden for RICs. Accordingly, the final regulation provides that RICs are not subject to the revised base period standard of these final regulations.

A similar exclusion from the revised base period standard has been made for REITs due to their similar distribution requirements. The regulation has also been amended to provide that the Service may by notice provide that the revised base period standard shall not apply to any section 988 transaction of an entity with distribution requirements similar to that of RICs and REITs.

In addition, the regulation was amended to provide that generally accepted accounting principles may not apply to alter the base period outlined in paragraph (f)(1)(ii)(A) of this section. This change is intended to clarify that the last sentence of § 1.985–1(b)(2)(ii)(D) may not be used to alter the base period for purposes of section 988.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedures Act (5 U.S.C. chapter 5) and the Regulatory Flexibility Act (5 U.S.C. chapter 6) do not apply to these regulations, and therefore, a Regulatory Flexibility Analysis is not required.

Drafting Information

The principal author of these regulations is John W. Rogers III of the Office of the Associate Chief Counsel (International). However, other personnel from the IRS and Treasury Department also participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

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

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

Par. 2. In § 1.988–1, paragraph (f) is revised to read as follows:

§ 1.988–1 Certain definitions and special rules.

* * * * *

(f) *Hyperinflationary currency*—(1) *Definition*—(i) *General rule.* For purposes of section 988, a hyperinflationary currency means a currency described in § 1.985–1(b)(2)(ii)(D). Unless otherwise provided, the currency in any example used in §§ 1.988–1 through 1.988–5 is not a hyperinflationary currency.

(ii) *Special rules for determining base period.* In determining whether a currency is hyperinflationary under § 1.985–1(b)(2)(ii)(D) for purposes of this paragraph (f), the following rules will apply:

(A) The base period means the thirty-six calendar month period ending on the last day of the taxpayer's (or qualified business unit's) current taxable year. Thus, for example, if for 1996, 1997, and 1998, a country's annual inflation rates are 6 percent, 11 percent, and 90 percent, respectively, the cumulative inflation rate for the three-year base period is 124% [$((1.06 \times 1.11 \times 1.90) - 1.0 = 1.24) \times 100 = 124\%$]. Accordingly, assuming the QBU has a calendar year as its taxable year, the currency of the country is hyperinflationary for the 1998 taxable year. This change in the § 1.985–1(b)(2)(ii)(D) base period shall not apply to any section 988 transaction of an entity described in section 851 (regulated investment company (RIC)) or section 856 (real estate investment trust (REIT)). The Service may, by notice, provide that the foregoing change in the § 1.985–1(b)(2)(ii)(D) base period does not apply to any section 988 transaction of an entity with distribution requirements similar to a RIC or REIT.

(B) The last sentence of § 1.985–1(b)(2)(ii)(D) shall not apply to alter the base period for purposes of this paragraph (f) in determining whether a currency is hyperinflationary for purposes of section 988. Accordingly, generally accepted accounting principles may not apply to alter the base period for purposes of this paragraph (f).

(2) *Effective date.* Paragraph (f)(1) of this section shall apply to transactions entered into after February 14, 2000.

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Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Approved: November 29, 2000.

Jonathan Talisman,

Acting Assistant Secretary of the Treasury.

[FR Doc. 00–32188 Filed 12–29–00; 8:45 am]

BILLING CODE 4810–31–P

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[TD 8930]

RINs 1545–AV14 and 1545–A051

Credit for Increasing Research Activities

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the computation of the credit under section 41(c) and the definition of *qualified research* under section 41(d). These regulations are intended to provide guidance concerning the requirements necessary to qualify for the credit for increasing research activities, guidance in computing the credit for increasing research activities, and rules for electing and revoking the election of the alternative incremental credit. These regulations reflect changes to section 41 made by the Tax Reform Act of 1986 (the 1986 Act), the Revenue Reconciliation Act of 1989, the Small Business Job Protection Act of 1996, the Taxpayer Relief Act of 1997, the Tax and Trade Relief Extension Act of 1998 (the 1998 Act), and the Tax Relief Extension Act of 1999 (the 1999 Act). These regulations also provide certain technical amendments to the existing regulations.

DATES: *Effective Dates:* These regulations are effective January 3, 2001.

Applicability Dates: For dates of applicability of these regulations, see Effective Dates under **SUPPLEMENTARY INFORMATION.**

FOR FURTHER INFORMATION CONTACT: Lisa J. Shuman or Leslie H. Finlow at (202) 622–3120 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collections of information contained in § 1.41–8(b) of this final rule have been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507) under the number 1545–1625. Responses to these collections of information are mandatory.

The reporting burden contained in § 1.41–8(b)(2) (relating to the election of the alternative incremental credit) is reflected in the burden of Form 6765.

Estimated average annual burden hours per respondent under § 1.41–8(b)(3) (relating to the revocation of the election to use the alternative incremental credit) is 250 hours.

Comments concerning the accuracy of this burden estimate and suggestions for reducing this burden should be sent to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, W:CAR:MP:FP:S:O, Washington, DC 20224, and 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.

The collections of information contained in § 1.41–4(d) of this final rule have been reviewed and, pending receipt and evaluation of public comments, approved by the Office of Management and Budget (OMB) under 44 U.S.C. 3507 and assigned control number 1545–1625. This information is required to assist in the examination of the research credit and to ensure that the research credit is properly targeted to serve as an incentive to engage in qualified research. This information will be used to verify that the amounts treated as qualified research expenses were paid or incurred for activities intended to discover information that exceeds, expands, or refines the common knowledge of skilled professionals in the relevant field of science or engineering. This collection of information is required to obtain a benefit. The likely recordkeepers are businesses or other for-profit institutions.

Estimated total annual recordkeeping burden for § 1.41–4(d) is 18,000 hours. The annual estimated burden per respondent varies from .5 hours to 2.5 hours, depending on the circumstances, with an estimated average of 1.5 hours.

The estimated number of recordkeepers is 12,000.

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, W:CAR:MP:FP:S:O,