DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[REG–131128–04]

RIN 1545–BD54

Guidance Under Section 1502; Miscellaneous Operating Rules for Successor Persons; Succession to Items of the Liquidating Corporation

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations under section 1502 that provide guidance regarding the manner in which the intercompany items of a liquidating member are succeeded to, and taken into account, in cases in which more than one distributee member acquires the assets of the liquidating corporation in a complete liquidation to which section 332 applies. This document also contains proposed regulations under section 1502 that provide guidance regarding the manner in which such distributee members succeed to the items (including items described in section 381(c)) of the liquidating corporation. These regulations apply to corporations filing consolidated returns.

DATES: Written or electronic comments and requests for a public hearing must be received by May 23, 2005.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG–131128–04), room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (REG–131128–04), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC, or sent electronically, via the IRS Internet site at *http://www.irs.gov/regs* or via the Federal eRulemaking Portal at *http://www.regulations.gov* (indicate IRS and REG–131128–04).

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Jeffrey B. Fienberg or Charles M. Levy (202) 622–7770; concerning submissions and the hearing, Sonya Cruse, (202) 622–4693 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background and Explanation of Provisions

The Complete Liquidation Rules

Section 332(a) provides that no gain or loss shall be recognized on the receipt by a corporation of property distributed in complete liquidation of another corporation. Section 332(b) provides, in part, that a distribution shall be considered to be in complete liquidation only if the corporation receiving such property was, on the date of the adoption of the plan of liquidation and at all times thereafter until the receipt of the property, the owner of stock that meets the requirements of section 1504(a)(2) and the distribution is made in complete cancellation or redemption of all of the stock of the liquidating corporation. Section 1.1502–34 provides that in determining the stock ownership of a member of a group in another corporation for purposes of determining the application of section 332(b), stock owned by all of the members of the group in that other corporation shall be aggregated. Therefore, for example, if one member of a group owns 60 percent of the stock of the liquidating corporation and another member of the group owns the remaining 40 percent of the stock of the liquidating corporation, section 332 will apply to the liquidation.

Section 337(a) provides that the liquidating corporation does not recognize gain or loss on the distribution to the 80-percent distributee of any property in a complete liquidation to which section 332 applies. For this purpose, the term ''80-percent distributee'' means only the corporation that meets the 80-percent stock ownership requirements of section 332(b). Under section 337(c), the determination of whether any corporation is an 80-percent distributee must be made without regard to any consolidated return regulation. Under section 336, if section 337(a) does not apply, the liquidating corporation must recognize gain or loss on the distribution of property in complete liquidation as if such property were sold to the distributee at its fair market value. Therefore, a liquidating distribution may be taxable to the distributing corporation and tax-free to the distributees.

The Intercompany Transaction Rules

Section 1.1502–13 prescribes rules for taking into account items of income, gain, deduction, and loss of members from intercompany transactions. The purpose of those rules is to clearly reflect the taxable income (and tax liability) of the group by preventing intercompany transactions from creating, accelerating, avoiding, or deferring consolidated taxable income or consolidated tax liability. Under § 1.1502–13(j)(2)(ii), if the assets of a member of the group are acquired by a successor member, the successor member succeeds to, and takes into account (under the rules of § 1.1502–13), the predecessor's intercompany items. In addition, if two or more successor members acquire assets of the predecessor, the successors take into account the predecessor's intercompany items in a manner that is consistently applied and reasonably carries out the purposes of § 1.1502–13 and applicable provisions of law. Section 1.1502–13(j)(2)(i) provides that any reference to a person includes, as the context may require, a reference to a predecessor or successor. For this purpose, a predecessor includes a transferor of assets to a transferee (the successor) in a transaction (A) to which section 381(a) applies; (B) in which substantially all of the assets of the transferor are transferred to members in a complete liquidation; or (C) in which the successor's basis in assets is determined (directly or indirectly, in whole or in part) by reference to the basis of the transferor, but the transferee is a successor only with respect to the assets the basis of which is so determined.

The current regulations include two examples that illustrate how these rules operate when a member of a group, X, engages in a complete liquidation in which it distributes its assets to S and B, also group members. In *example 6* of § 1.1502–13(j)(9), S owns 100 percent of the common stock of X and, therefore, is an 80-percent distributee without regard to the application of § 1.1502–34. B owns 100 percent of the preferred stock of X, which is described in section 1504(a)(4), and, therefore, is an 80-percent distributee only by reason of the application of § 1.1502–34. X recognizes gain on the assets distributed to B. That gain, however, is not taken into account as a result of the liquidation and S succeeds to that gain.

In *example 7* of § 1.1502–13(j)(9), S owns 60 percent of the X stock and B owns 40 percent of the X stock. Therefore, both S and B are 80-percent distributees only by reason of the application of § 1.1502–34. X recognizes gain on the assets distributed to both S and B. That gain, however, is not taken into account as a result of the liquidation and S succeeds to X's gain on the assets distributed to B and B succeeds to X's gain on the assets distributed to S. As a result, under the acceleration rule, on the deconsolidation of either S or B, those gains would be taken into account in their entirety.

The rules illustrated by the examples reflect the concern that, under prior intercompany regulations, the assets of

an acquired corporation could be broken up without a corporate level tax. See 59 FR 18011. The IRS and Treasury Department have re-examined the current regulations and have concluded that accelerating all of the intercompany gains recognized on the liquidation of the liquidating corporation's assets in these cases is not necessary to deter mirror subsidiary transactions. Therefore, these regulations propose that each member of the group to which assets of a liquidating member are transferred succeeds to, and takes into account, the intercompany items of the liquidating member that are generated in the liquidation to the extent such items would have been reflected in investment basis adjustments to the stock of the liquidating member owned by such distributee member under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, any stock of the liquidating member owned by nonmembers had been redeemed by the liquidating member in exchange for the money or property distributed to that nonmember in the liquidating distribution, and then such items had been taken into account under § 1.1502–13(d).

These proposed regulations also address the manner in which the distributee members succeed to the intercompany items of the liquidating member that were not generated in the liquidating transaction. The IRS and Treasury Department have not identified a policy reason to distinguish between intercompany items that are generated in the liquidating transaction and intercompany items that are generated prior to the liquidating transaction. Therefore, these proposed regulations adopt the same rule for both of these categories of intercompany items.

Application of Section 381

Section 381(a)(1) provides that the acquiring corporation in a distribution to which section 332 applies shall succeed to, and take into account, the items of the distributor corporation (*i.e.*, liquidating corporation) that are listed in section 381(c). Section 1.381(a)–1(b)(2) provides that only a single corporation can be an acquiring corporation for purposes of section 381. Currently, there are no rules that govern which corporation succeeds to the items of the liquidating corporation when section 332 applies to more than one distributee as may happen by reason of the application of § 1.1502–34 when the distributees are members of the same consolidated group. These proposed regulations include such rules.

The IRS and Treasury Department believe that it is appropriate for each distributee member, even if it is not an 80-percent distributee without regard to the application of § 1.1502–34, to succeed to items of the liquidating corporation that could be used to offset the income or tax liability of the group or any member. If the liquidating corporation is a member of the group, any income or gain recognized by the liquidating corporation in connection with the liquidation will be deferred under § 1.1502–13. If § 1.1502–13 did not apply, that income or gain could be offset by net operating losses of the liquidating corporation or, alternatively, any tax liability resulting from the recognition of that income or gain could be offset by credits of the liquidating corporation. The operation of § 1.1502–34 should not change that result. Single entity principles should control in situations in which section 332 applies to the distributee members. Therefore, these proposed regulations provide that each distributee member succeeds to the items of the liquidating corporation that could be used to offset the income or tax liability of the group or any member (including net operating loss carryovers and capital loss carryovers) to the extent that such items would have been reflected in investment basis adjustments to the stock of the liquidating corporation owned by such distributee member under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, any stock of the liquidating corporation owned by nonmembers had been redeemed and then such items had been taken into account. In addition, each distributee member succeeds to the credits of the liquidating corporation (including credits under sections 38 and 53) to the extent that the items of gain, income, loss, or deduction attributable to the activities that gave rise to the credit would have been reflected in investment basis adjustments to the stock of the liquidating corporation owned by such distributee member under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, any stock of the liquidating corporation owned by nonmembers had been redeemed and then such items had been taken into account. For this purpose, if the liquidating corporation is not a member of the group at the time of the liquidation, these rules are applied as if the liquidating corporation had been a member of the group at that time. Finally, except to the extent that the distributee member's earnings and profits already reflect the liquidating corporation's earnings and profits, these proposed regulations provide that the earnings and profits of the liquidating corporation are allocated to each distributee member under the principles of § 1.1502–32(c), treating any stock of the liquidating corporation owned by nonmembers as if it had been redeemed immediately prior to the liquidation.

With respect to items other than those that can offset the income or tax liability of the group or any member and earnings and profits, these proposed regulations provide that a distributee member that, immediately prior to the liquidation, satisfies the requirements of section 1504(a)(2) without regard to § 1.1502–34 succeeds to the items of the liquidating corporation in accordance with the principles set forth in the Code (including section 381) and the regulations promulgated thereunder. This rule is consistent with the treatment of a nonconsolidated corporation that satisfies the ownership requirements of section 1504(a)(2) with respect to a liquidating corporation.

Finally, again with respect to items other than those that can offset the income or tax liability of the group or any member and earnings and profits, these proposed regulations provide that a distributee member that, immediately prior to the liquidation, does not own stock in the liquidating corporation meeting the requirements of section 1504(a)(2) without regard to § 1.1502–34 succeeds to items of the liquidating corporation to the extent that it would have succeeded to those items if it had purchased, in a taxable transaction, the assets or businesses of the liquidating corporation that it received in the liquidation and assumed the liabilities it assumed in the liquidation. As described above, pursuant to section 336, to the extent that section 337(a) does not apply, a liquidating corporation must recognize gain or loss on the distribution of property in complete liquidation as if such property were sold to the distributee at its fair market value. Although no provision of the Code states that the distributee is the purchaser of those assets, the IRS and Treasury Department believe that it is reasonable to treat the distributee as purchasing those assets for purposes of determining the attributes to which such a distributee succeeds.

Proposed Effective Date

These regulations are proposed to apply to complete liquidations that occur after the date that these regulations are published as final regulations in the **Federal Register**.

Special Analyses

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

Comments and Requests for Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal author of these proposed regulations is Jeffrey B. Fienberg of the Office of Associate Chief Counsel (Corporate). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

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 * * *

§ 1.1502–13 also issued under 26 U.S.C. 1502. * * *

§ 1.1502–80 also issued under 26 U.S.C. 1502.* * *

Par. 2. Section 1.1502–13 is amended by:

1. Adding a sentence at the end of paragraph (j)(2)(ii).
2. Adding paragraph (j)(2)(iii).
3. Redesignating paragraph (j)(9) introductory text as paragraph (j)(9)(i).
4. Revising *Example* 6 and *Example 7* of newly designated paragraph (j)(9)(i).
5. Adding paragraph (j)(9)(ii).

The revisions and additions read as follows:

§ 1.1502–13 Intercompany transactions.

* * * * *

(j) * * *

(2) * * *

(ii) *Intercompany items.* * * * For example, if the assets of a predecessor are acquired by more than one successor in a transaction to which section 381(a)(1) applies, each successor succeeds to, and takes into account (under the rules of this section), each of the predecessor's intercompany items (whether resulting from distributions in liquidation or otherwise) to the extent that such items would have been reflected in investment basis adjustments to the stock of the predecessor owned by that successor under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, any stock of the predecessor owned by nonmembers had been redeemed in exchange for the money or property distributed to that nonmember in the transaction to which section 381(a)(1) applies, and then such items had been taken into account under § 1.1502–13(d).

(iii) *Effective date.* The third sentence of paragraph (j)(2)(ii) of this section applies to transactions occurring after the date these regulations are published as final regulations in the **Federal Register**.

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(9) *Examples.* (i) The operating rules of this paragraph (j) are illustrated generally throughout this section, and by the following examples:

* * * * *

Example 6. Liquidation—80% distributee. (i) *Facts.* B1, B2, and S are members of the same consolidated group. S has only common stock outstanding. B1 owns 80% of S's stock, and B2 owns the remaining 20%. On January 1 of Year 2, S sells two assets to another member of the group. S recognizes $100 of gain with respect to the first asset and $100 of loss with respect to the second asset. On July 1 of Year 3, S distributes all of its remaining assets to B1 and B2 in a complete liquidation. At the time of the liquidation, S's assets have an aggregate basis of $0 and an aggregate value of $100, and neither the gain nor the loss from the prior two asset sales has been taken into account under this section. Under § 1.1502–34, section 332 applies to both B1 and B2. Under section 337, S has no gain or loss from its liquidating distribution to B1. Under sections 336 and 337(c), S has a $20 gain from its liquidating distribution to B2. On January 1 of Year 4, B2 ceases to be a member of the group.

(ii) *Succession to intercompany items.* Under the matching rule, S's $20 gain from its liquidating distribution to B2 is not taken into account under this section as a result of the liquidation (and, therefore, is not yet reflected under §§ 1.1502–32 and 1.1502–33). Under the successor person rule of paragraph (j)(2)(i) of this section, B1 and B2 are both successors to S. Under paragraph (j)(2)(ii) of this section, B1 and B2 each succeeds to S's intercompany items to the extent that such items would have been reflected in investment basis adjustments to its stock of S under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, such items had been taken into account under § 1.1502–13(d). Therefore, B1 succeeds to 80% of the $20 of intercompany gain from the assets distributed to B2 in the liquidation, and 80% of the $100 of intercompany gain and 80% of the $100 of intercompany loss from the assets that S sold prior to the liquidation. In addition, B2 succeeds to 20% of the $20 of intercompany gain from the assets distributed to B2 in the liquidation and 20% of the $100 of intercompany gain and 20% of the $100 of intercompany loss from the assets that S sold prior to the liquidation.

(iii) *Taking into account intercompany items.* S's gain from its liquidating distribution to B2 and S's gain and loss from the sale of the two assets prior to the liquidation will be taken into account by B1 and B2 under the matching and acceleration rules of this section based on subsequent events. Therefore, in connection with B2 ceasing to be a member of the group, B1 will take into account $16 of the intercompany gain from the assets distributed to B2 in the liquidation. In addition, B2 will take into account $4 of the intercompany gain from the assets distributed to B2 in the liquidation and $20 of the intercompany gain and $20 of the intercompany loss from the two assets that S sold prior to the liquidation.

Example 7. Liquidation—no 80% distributee. (i) *Facts.* B1, B2, and S are members of the same consolidated group. S has only common stock outstanding. B1 and B2 each owns 40% of S's stock, and A, a nonmember, owns the remaining 20% of S's stock. On January 1 of Year 2, S sells two assets to another member of the group. S recognizes $100 of gain with respect to the first asset and $100 of loss with respect to the second asset. On July 1 of Year 3, S distributes all of its remaining assets to B1, B2, and A in complete liquidation. At the

time of the liquidation, S's assets have an aggregate basis of $0 and an aggregate value of $100, and neither the gain nor the loss from the prior two asset sales has been taken into account under this section. Under § 1.1502–34, section 332 applies to both B1 and B2. Under sections 336 and 337(c), S has a $100 gain from its liquidating distributions to B1, B2, and A.

(ii) *Succession to intercompany items.* Under the matching rule, S's $80 gain from its liquidating distributions to B1 and B2 is not taken into account under this section as a result of the liquidation (and, therefore, is not yet reflected under §§ 1.1502–32 and 1.1502–33). Under the successor person rule of paragraph (j)(2)(i) of this section, B1 and B2 are successors to S. Under paragraph (j)(2)(ii) of this section, B1 and B2 each succeeds to S's intercompany items to the extent that such items would have been reflected in investment basis adjustments to its stock of S under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, the stock of S owned by A had been redeemed in exchange for the money or property distributed to A in the liquidation, and then such items had been taken into account under § 1.1502–13(d). If A had been redeemed, then S's items would have produced investment basis adjustments in the stock of S owned by each of B1 and B2 equally. Therefore, each of B1 and B2 succeeds to 50% of the $80 of intercompany gain from the assets distributed to B1 and B2 in the liquidation and 50% of the $100 of intercompany gain and 50% of the $100 of intercompany loss from the assets that S sold prior to the liquidation. S's $20 gain with respect to the assets that are distributed to A in the liquidation is taken into account immediately.

(iii) *Taking into account intercompany items.* S's gain from its liquidating distributions to B1 and B2 and S's gain and loss from the sale of the two assets prior to the liquidation will be taken into account by B1 and B2 under the matching and acceleration rules of this section based on subsequent events.

(ii) *Effective dates.* Paragraph (j)(9)(i) *Examples 6* and *7* apply to transactions occurring after the date these regulations are published as final regulations in the **Federal Register**.

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Par. 3. Section 1.1502–80 is amended by:

1. Removing the second sentence from paragraph (a).

2. Adding paragraph (g).

The addition reads as follows:

§ 1.1502–80 Applicability of other provisions of law.

* * * * *

(g) *Special rules for liquidations to which section 332 applies.* Notwithstanding the general rule of section 381, if one or more members is a distributee of assets in a liquidation to which section 332 applies and such member or members in the aggregate own stock of the liquidating corporation that satisfies the requirements of section 1504(a)(2) (regardless of whether any single member owns stock in the liquidating corporation that satisfies the requirements of section 1504(a)(2)), such member or members shall succeed to the items (including items described in section 381(c)) of the liquidating corporation, to the extent not otherwise prohibited by any applicable provision of law, as provided in this paragraph (g).

(1) Each distributee member shall succeed to the items of the liquidating corporation that could be used to offset the income or tax liability of the group or any member (including net operating loss carryovers and capital loss carryovers) to the extent that such items would have been reflected in investment basis adjustments to the stock of the liquidating corporation owned by such distributee member under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, any stock of the liquidating corporation owned by nonmembers had been redeemed and then such items had been taken into account. In addition, each distributee member shall succeed to the credits of the liquidating corporation (including credits under sections 38 and 53) to the extent that the items of gain, income, loss, or deduction attributable to the activities that gave rise to the credit would have been reflected in investment basis adjustments to the stock of the liquidating corporation owned by such distributee member under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, any stock of the liquidating corporation owned by nonmembers had been redeemed and then such items had been taken into account. If the liquidating corporation is not a member of the group at the time of the liquidation, the previous two sentences shall be applied as if the liquidating corporation had been a member of the group at the time of the liquidation. Finally, except to the extent that the distributee member's earnings and profits already reflect the liquidating corporation's earnings and profits, the earnings and profits of the liquidating corporation are allocated to each distributee member under the principles of § 1.1502–32(c), treating any stock of the liquidating corporation owned by nonmembers as if it had been redeemed immediately prior to the liquidation.

(2) With regard to items to which paragraph (g)(1) of this section does not apply, a distributee member that, immediately prior to the liquidation, owns stock in the liquidating corporation meeting the requirements of section 1504(a)(2) without regard to § 1.1502–34 shall succeed to items of the liquidating corporation in accordance with section 381 and other applicable principles.

(3) With regard to items to which paragraph (g)(1) of this section does not apply, a distributee member that, immediately prior to the liquidation, does not own stock in the liquidating corporation meeting the requirements of section 1504(a)(2) without regard to § 1.1502–34 shall succeed to items of the liquidating corporation to the extent that it would have succeeded to those items if it had purchased, in a taxable transaction, the assets or businesses of the liquidating corporation that it received in the liquidation and assumed the liabilities it assumed in the liquidation.

(4) *Examples.* The following examples illustrate the application of this paragraph (g):

Example 1. Liquidation—80% distributee.

(i) *Facts.* X has only common stock outstanding. On January 1 of Year 1, X acquired equipment with a 10-year life and elected to depreciate the equipment using the straight-line method of depreciation. On January 1 of Year 7, B1 and B2 own 80% and 20%, respectively, of X's stock. X is a domestic corporation but is not a member of the group that includes B1 and B2. On that date, X distributes all of its assets to B1 and B2 in complete liquidation. The equipment is distributed to B1. Under section 334(b), B1's basis in the equipment is the same as it would be in X's hands. After computing its tax liability for the taxable year that includes the liquidation, X has net operating losses of $100, business credits of $40, and earnings and profits of $80.

(ii) *Succession to items described in section 381(c).* Under paragraph (g)(1) of this section, B1 and B2 each succeeds to X's items that could be used to offset the income or tax liability of the group or any member to the extent that such items would have been reflected in investment basis adjustments to the stock of X it owned under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, such items had been taken into account. Accordingly, B1 and B2 succeed to $80 and $20, respectively, of X's net operating loss. In addition, under paragraph (g)(1) of this section, because, immediately prior to the liquidation, 80% of the items of gain, income, loss, or deduction attributable to the activities that gave rise to the business credits of $40 would have been reflected in investment basis adjustments to the stock of X owned by B1 under the principles of § 1.1502–32(c) and 20% of those items would have been reflected in investment basis adjustments to the stock of X owned by B2 under those same principles, B1 and B2 succeed to $32 and $8, respectively, of X's business credits. Under paragraph (g)(1) of this section, because B1's and B2's earnings and profits do not reflect X's earnings and profits, X's earnings and profits are allocated to B1 and B2 under the principles of § 1.1502–32(c). Therefore, B1 and B2 succeed

to $64 and $16, respectively, of X's earnings and profits. Finally, because B1 owns stock in X meeting the requirements of section 1504(a)(2) without regard to § 1.1502–34, under paragraph (g)(2), B1 is required to continue to depreciate the equipment using the straight-line method of depreciation.

Example 2. Liquidation—no 80% distributee.

(i) *Facts.* The facts are the same as in Example 1 except that B1 and B2 own 60% and 40%, respectively, of X's stock. Therefore, under section 334(a), B1's basis in the equipment is its fair market value at the time of the distribution. In addition, on January 1 of Year 6, X entered into a long-term contract with Y, an unrelated party. The total contract price is $1000, and X estimates the total allocable contract costs to be $500. At the time of the liquidation, X had received $250 in progress payments under the contract and incurred costs of $125. X accounted for the contract under the percentage of completion method described in section 460(b). In the liquidation, B1 assumes X's contract obligations and rights.

(ii) *Succession to items described in section 381(c).* (A) *Losses and credits.* Under paragraph (g)(1) of this section, B1 and B2 each succeeds to X's items that could be used to offset the income or tax liability of the group or any member to the extent that such items would have been reflected in investment basis adjustments to the stock of X it owned under the principles of § 1.1502–32(c) if, immediately prior to the liquidation, such items had been taken account. Accordingly, B1 and B2 succeed to $60 and $40, respectively, of X's net operating loss. In addition, under paragraph (g)(1) of this section, because, immediately prior to the liquidation 60% of the items of gain, income, loss, or deduction attributable to the activities that gave rise to the business credits of $40 would have been reflected in investment basis adjustments to the stock of X owned by B1 under the principles of § 1.1502–32(c) and 40% of those items would have been reflected in the investment basis adjustments to the stock of X owned by B2 under those same principles, B1 and B2 succeed to $24 and $16, respectively, of X's business credits.

(B) *Earnings and profits.* Under paragraph (g)(1) of this section, because B1's and B2's earnings and profits do not reflect X's earnings and profits, X's earnings and profits are allocated to B1 and B2 under the principles of § 1.1502–32(c). Therefore, B1 and B2 succeed to $48 and $32, respectively, of X's earnings and profits.

(C) *Depreciation of equipment's basis.* By reason of section 168(i)(7), to the extent that B1's basis in the equipment does not exceed X's basis in the equipment, B1 will be required to continue to depreciate the equipment using the straight-line method of depreciation.

(D) *Method of accounting for long-term contract.* Under paragraph (g)(3) of this section, B1 does not succeed to X's method of accounting for the contract. Rather, under § 1.460–4(k)(2), B1 is treated as having entered into a new contract on the date of the liquidation. Under § 1.460–4(k)(2)(iii), B1 must evaluate whether the new contract should be classified as a long-term contract within the meaning of § 1.460–1(b) and account for the contract under a permissible method of accounting.

(5) *Effective date.* Paragraph (g) applies to transactions occurring after the date these regulations are published as final regulations in the **Federal Register**.

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Mark E. Matthews,

Deputy Commissioner for Services and Enforcement.

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DEPARTMENT OF THE INTERIOR

Minerals Management Service

30 CFR Part 206

RIN 1010–AD00

Public Workshop on Proposed Rule—Establishing Oil Value for Royalty Due on Indian Leases

AGENCY: Minerals Management Service, Interior.

ACTION: Notice of public workshops.

SUMMARY: The Minerals Management Service (MMS) is giving notice of public workshops concerning the valuation of crude oil produced from Indian oil and gas leases.

DATES: The public workshop dates are:

Workshop 1: Oklahoma City, Oklahoma, on March 8, 2005, beginning at 8:30 a.m. and ending at 2 p.m., central time.

Workshop 2: Albuquerque, New Mexico, on March 9, 2005, beginning at 8:30 a.m. and ending at 2 p.m., mountain time.

Workshop 3: Billings, Montana, on March 16, 2005, beginning at 8:30 a.m. and ending at 2 p.m., mountain time.

ADDRESSES: Public workshop locations:

Workshop 1 will be held at the Sheraton Downtown in the Frontier Room, One North Broadway, Oklahoma City, Oklahoma 73102 (telephone number (405) 235–2780).

Workshop 2 will be held at the Wyndham Albuquerque in the Bernalillo Room, 2910 Yale Boulevard SE., Albuquerque, New Mexico 87106 (telephone number (505) 843–7000).

Workshop 3 will be held at the Sheraton Billings Hotel in the Avalanche Room, 27 North 27th Street, Billings, Montana 59101 (telephone number (406) 252–7400).

FOR FURTHER INFORMATION CONTACT: Mr. John Barder, Supervisory Mineral Revenue Specialist, Minerals Management Service, Minerals Revenue Management, Indian Oil and Gas Compliance and Asset Management, telephone (303) 231–3702, Fax (303) 231–3755, e-mail to *John.Barder@mms.gov,* P.O. Box 25165, MS 396B2, Denver, Colorado 80225–0165.

SUPPLEMENTARY INFORMATION: On February 12, 1998, MMS published a notice of proposed rulemaking regarding the value for royalty purposes of crude oil produced from Indian tribal and allotted leases. 63 FR 7089. On January 5, 2000, MMS published a supplementary proposed Indian oil valuation rule. 65 FR 403. Because of the substantial amount of time that has passed since the last proposal, and because of changes that have occurred since then in the market for crude oil, MMS has decided not to promulgate a final rule based on the previous proposed rules and comments received. Therefore, MMS is withdrawing both the proposed rule and the supplementary proposed rule, and is starting a new rulemaking process regarding the royalty valuation of crude oil produced from Indian leases.

The record compiled for the February 1998 proposed rule and the January 2000 supplementary proposed rule, including comments submitted on those proposals, will not be part of the record of the new rulemaking. At this time, MMS has made no decisions regarding the content of a future proposed rule or any future final rule that may result from this process. A new proposed rule may or may not include provisions similar to prior proposals.

The MMS has decided to gather preliminary comments and conduct preliminary consultation in anticipation of publishing a new proposed rule regarding Indian oil royalty valuation. The MMS is conducting the series of public workshops identified above for that purpose.

Among other things, MMS specifically seeks public comment on the following issues:

1. The MMS published amendments to the Federal crude oil valuation rule on May 5, 2004 (69 FR 24959). Should MMS adopt any of those same changes in the Indian oil valuation rule (*e.g.*, using NYMEX prices adjusted for location and quality and for transportation costs for oil that is not sold at arm's length, and using 1.3 times the Standard & Poor's BBB bond rate as the rate of return on undepreciated capital investment in calculating non-arm's-length transportation costs)?

2. The current Indian oil valuation rule provides that Amajor portion''