Bulletin No. 1996–34
August 19, 1996

HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

SPECIAL ANNOUNCEMENT

Announcement 96–75, page 29.
A public hearing will be held on September 4, 1996, on issues related to a study of ''global interest netting'' being conducted by the Internal Revenue Service and Treasury.

INCOME TAX

Rev. Rul. 96–39, page 4.
LIFO; price indexes; department stores. The June 1996 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, June 30, 1996.

Ct.D. 2058, page 13.
Refund claims; Tax Court; return not filed. The Tax Court lacks jurisdiction to award a refund of taxes paid more than two years before the date the taxpayer was mailed a notice of deficiency, if, on the date that the notice was mailed, the taxpayer had not yet filed a return. In these circumstances, the applicable look-back period under section 6512 of the Code is two years. **Commissioner of Internal Revenue v. Robert F. Lundy.**

Ct.D. 2059, page 10.
Validity of liens; bankruptcy. A bankruptcy court may not equitably subordinate claims on a categorical basis in derogation of Congress' priorities scheme. **United States v. Thomas R. Noland.**

FI–32–95, page 21.
Proposed regulations under section 475 of the Code make mark-to-market accounting inapplicable to most equity interests in related entities. A public hearing will be held on October 15, 1996.

CO–9–96, page 20.
Proposed regulations under section 1059 of the Code relate to certain distributions made by corporations to certain corporate shareholders. A public hearing will be held on October 2, 1996.

PS–39–93, page 27.
Proposed regulations under section 280B of the Code relate to deductions available upon demolition of a building. A public hearing will be held on October 9, 1996.

Announcement 96–76, page 29.
Rev. Proc. 96–36, 1996–27 I.R.B. 11, which provides specifications for filing Forms 1098, 1099, 5498, and W–2G, is corrected.

Pub. L. 104–117, page 19.
An Act to provide that members of the Armed Forces performing services for the peacekeeping efforts in Bosnia and Herzegovina, Croatia, and Macedonia shall be entitled to tax benefits in the same manner as if such services were performed in a combat zone, and for other purposes, is reproduced.

EXCISE TAX

Ct.D. 2060, page 5.
Foreign insurance taxes. The Export Clause prohibits assessment of nondiscriminatory federal taxes on goods in export transit. **United States v. International Business Machines Corp.**

Finding Lists begin on page 32.

Mission of the Service

The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost; serve the public by continually improving the quality of our products and services; and perform in a manner warranting the highest degree of public confidence in our integrity, efficiency and fairness.

Statement of Principles of Internal Revenue Tax Administration

The function of the Internal Revenue Service is to administer the Internal Revenue Code. Tax policy for raising revenue is determined by Congress.

With this in mind, it is the duty of the Service to carry out that policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.

At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he or she is ''protecting the revenue.'' The revenue is properly protected only when we ascertain and apply the true meaning of the statute.

The Service also has the responsibility of applying and administering the law in a reasonable, practical manner. Issues should only be raised by examining officers when they have merit, never arbitrarily or for trading purposes. At the same time, the examining officer should never hesitate to raise a meritorious issue. It is also important that care be exercised not to raise an issue or to ask a court to adopt a position inconsistent with an established Service position.

Administration should be both reasonable and vigorous. It should be conducted with as little delay as possible and with great courtesy and considerateness. It should never try to overreach, and should be reasonable within the bounds of law and sound administration. It should, however, be vigorous in requiring compliance with law and it should be relentless in its attack on unreal tax devices and fraud.

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly and may be obtained from the Superintendent of Documents on a subscription basis. Bulletin contents of a permanent nature are consolidated semiannually into Cumulative Bulletins, which are sold on a single-copy basis.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
With the exception of the Notice of Proposed Rulemaking and the disbarment and suspension list included in this part, none of these announcements are consolidated in the Cumulative Bulletins.

The first Bulletin for each month includes an index for the matters published during the preceding month. These monthly indexes are cumulated on a quarterly and semiannual basis, and are published in the first Bulletin of the succeeding quarterly and semi-annual period, respectively.

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Part I. Rulings and Decisions Under the Internal Revenue Code of 1986

Section 472.—Last-in, First-out Inventories

26 CFR 1.472–1: Last-in, first-out inventories.

LIFO; price indexes; department stores. The June 1996 Bureau of Labor Statistics price indexes are accepted for use by department stores employing the retail inventory and last-in, first-out inventory methods for valuing inventories for tax years ended on, or with reference to, June 30, 1996.

Rev. Rul. 96–39

The following Department Store Inventory Price Indexes for June 1996 were issued by the Bureau of Labor Statistics on July 16, 1996. The indexes are accepted by the Internal Revenue Service, under § 1.472–1(k) of the Income Tax Regulations and Rev. Proc. 86–46, 1986–2 C.B. 739, for appropriate application to inventories of department stores employing the retail inventory and last-in, first-out inventory methods for tax years ended on, or with reference to, June 30, 1996.

The Department Store Inventory Price Indexes are prepared on a national basis and include (a) 23 major groups of departments, (b) three special combinations of the major groups—soft goods, durable goods, and miscellaneous goods, and (c) a store total, which covers all departments, including some not listed separately, except for the following: candy, foods, liquor, tobacco, and contract departments.

BUREAU OF LABOR STATISTICS, DEPARTMENT STORE
INVENTORY PRICE INDEXES BY DEPARTMENT GROUPS
(January 1941 = 100, unless otherwise noted)

Groups	June 1995	June 1996	Percent Change from June 1995 to June 1996[1]
1. Piece Goods	522.9	551.1	5.4
2. Domestics and Draperies	646.7	641.0	−0.9
3. Women's and Children's Shoes	624.2	649.3	4.0
4. Men's Shoes	919.3	895.4	−2.6
5. Infants' Wear	587.9	627.1	6.7
6. Women's Underwear	515.1	535.4	3.9
7. Women's Hosiery	283.3	288.0	1.7
8. Women's and Girls' Accessories	549.5	545.5	−0.7
9. Women's Outerwear and Girls' Wear	416.3	401.1	−3.7
10. Men's Clothing	597.5	612.2	2.5
11. Men's Furnishings	562.4	584.5	3.9
12. Boys' Clothing and Furnishings	477.8	485.7	1.7
13. Jewelry	1004.9	1011.5	0.7
14. Notions	758.7	774.1	2.0
15. Toilet Articles and Drugs	859.9	877.8	2.1
16. Furniture and Bedding	663.1	673.6	1.6
17. Floor Coverings	577.0	576.4	−0.1
18. Housewares	771.8	808.7	4.8
19. Major Appliances	247.2	245.5	−0.7
20. Radio and Television	82.1	79.3	−3.4
21. Recreation and Education[2]	114.0	112.8	−1.1
22. Home Improvements[2]	122.6	127.4	3.9
23. Auto Accessories[2]	106.8	107.5	0.7
Groups 1–15: Soft Goods	587.8	592.4	0.8
Groups 16–20: Durable Goods	462.8	469.7	1.5
Groups 21–23: Misc. Goods[2]	113.9	113.7	−0.2
Store Total[3]	545.8	550.3	0.8

[1]Absence of a minus sign before percentage change in this column signifies price increase.
[2]Indexes on a January 1986=100 base.
[3]The store total index covers all departments, including some not listed separately, except for the following: candy, foods, liquor, tobacco, and contract departments.

DRAFTING INFORMATION

The principal author of this revenue ruling is Stan Michaels of the Office of Assistant Chief Counsel (Income Tax and Accounting). For further information regarding this revenue ruling, contact Mr. Michaels on (202) 622–4970 (not a toll-free call).

Section 4371.—Imposition of Tax

Ct.D. 2060

SUPREME COURT OF THE UNITED STATES

No. 95–591

UNITED STATES, PETITIONER v. INTERNATIONAL BUSINESS MACHINES CORPORATION

[517 U.S.—]

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

June 10, 1996

Syllabus

Pursuant to § 4371 of the Internal Revenue Code, respondent International Business Machines Corporation (IBM) paid a tax on insurance premiums remitted to foreign insurers to cover shipments of goods to its foreign subsidiaries. When its refund claims were denied, IBM filed suit in the Court of Federal Claims, contending that § 4371's application to policies insuring export shipments violated the Export Clause, which states that "[n]o Tax or Duty shall be laid on Articles exported from any State." The court agreed, rejecting the Government's argument that *Thames & Mersey Marine Ins. Co.* v. *United States,* 237 U. S. 19—in which this Court held that a federal stamp tax on policies insuring marine risks could not, under the Export Clause, be constitutionally applied to policies covering export shipments—had been superseded by subsequent decisions interpreting the Import-Export Clause, which states in relevant part, "No State shall . . . lay any Imposts or Duties on Imports or Exports." The Court of Appeals affirmed.

Held: The Export Clause prohibits assessment of nondiscriminatory federal taxes on goods in export transit.

(a) While this Court has strictly enforced the Export Clause's prohibition against federal taxation of goods in export transit and certain closely related services and activities, see, *e.g., Thames & Mersey, supra,* it has not exempted pre-export goods and services from ordinary tax burdens or exempted from federal taxation various services and activities only tangentially related to the export process, see, *e.g., Cornell* v. *Coyne*, 192 U.S. 418. Conceding that the tax assessed here violates the Export Clause under *Thames & Mersey*, the Government asks that the case be overruled because its underlying theory has been rejected in the context of the Commerce and Import-Export Clauses and those Clauses have historically been interpreted in harmony with the Export Clause.

(b) When this Court expressly disavowed its early view that the dormant Commerce Clause required a strict ban on state taxation of interstate commerce, *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274, 288–289, it resolved a long struggle over the meaning of the nontextual negative command of that Clause. The Export Clause, on the other hand, expressly prohibits Congress from laying any tax or duty on exports. These textual disparities strongly suggest that shifts in the Court's view of the dormant Commerce Clause's scope cannot govern Export Clause interpretation. Cf. *Richfield Oil Corp.* v. *State Bd. of Equalization*, 329 U. S. 69, 75–76.

(c) While one may question *Thames & Mersey*'s finding that a tax on policies insuring exports is functionally the same as a tax on exportation itself, the Government apparently has chosen not to do so here. Under the principles that animate the policy of *stare decisis*, the Court declines to overrule *Thames & Mersey*'s long-standing precedent, which has caused no uncertainty in commercial export transactions, on a theory not argued by the parties.

(d) This Court's recent Import-Export Clause cases do not require that *Thames & Mersey* be overruled. Meaningful textual differences that should not be overlooked exist between the Export Clause and the Import-Export Clause. In finding the assessments in *Michelin Tire Corp.* v. *Wages*, 423 U.S. 276, and *Department of Revenue of Wash.* v. *Association of Wash. Stevedoring Cos.*, 435 U. S. 734, valid, the Court recognized that the Import-Export Clause's absolute ban on "Imposts or Duties" is not a ban on every tax. Because impost and duty are thus narrower terms than tax, a particular state assessment might be beyond the Import-Export Clause's reach, while an identical federal assessment might be subject to the Export Clause. The word "Tax" has a common, and usually expansive, meaning that should not be ignored. The Clauses were also intended to serve different goals. The Government's policy argument—that the Framers intended the Export Clause to narrowly alleviate the fear of northern repression through taxation of southern exports by prohibiting only discriminatory taxes—cannot be squared with the Clause's broad language. The better reading is that the Framers sought to alleviate their concerns by completely denying to Congress the power to tax exports at all. See *Fairbank* v. *United States*, 181 U. S. 283.

(e) Even assuming that *Michelin* and *Washington Stevedoring* govern the Export Clause inquiry here, those holdings do not interpret the Import-Export Clause to permit assessment of nondiscriminatory taxes on imports and exports in transit.

59 F. 3d 1234, affirmed.

THOMAS, J., delivered the opinion of the Court, in which REHNQUIST, C. J., and O'CONNOR, SCALIA, SOUTER, and BREYER, JJ., joined. KENNEDY, J., filed a dissenting opinion, in which GINSBURG, J., joined. STEVENS, J., took no part in the consideration or decision of the case.

JUSTICE THOMAS delivered the opinion of the Court.

We resolve in this case whether the Export Clause of the Constitution permits the imposition of a generally applicable, nondiscriminatory federal tax on goods in export transit. We hold that it does not.

I

Section 4371 of the Internal Revenue Code imposes a tax on insurance premiums paid to foreign insurers that are not subject to the federal income tax.[1] 26 U. S. C. § 4371 (1982 ed.). International Business Machines Corporation (IBM) ships products that it manufactures in the United States to numerous foreign subsidiaries and insures those shipments against loss. When the foreign subsidiary makes the shipping arrangements, the subsidiary often places the insurance with a foreign carrier. When it does, both IBM and the subsidiary are listed as beneficiaries in the policy.

IBM filed federal excise tax returns for the years 1975 through 1984, but reported no liability under § 4371. The IRS audited IBM and determined that the premiums paid to foreign insurers were taxable under § 4371 and that IBM—as a named beneficiary of the insurance policies—was liable for the tax. The IRS assessed a tax against IBM for each of those years.

IBM paid the assessments and filed refund claims, which the IRS denied. IBM then commenced suit in the Court of Federal Claims, contending that application of § 4371 to policies insuring its export shipments violated the Export Clause. The focus of the suit was this Court's decision in *Thames & Mersey Marine Ins. Co.* v. *United States*, 237 U.S. 19 (1915), in which we held that a federal stamp tax on policies insuring marine risks could not, under the Export Clause, be constitutionally applied to policies covering export shipments. The United States argued that the analysis of *Thames & Mersey* is no longer valid, having been superseded by subsequent decisions interpreting the Import-Export Clause—specifically, *Michelin Tire Corp.* v. *Wages*, 423 U. S. 276 (1976), and *Department of Revenue of Wash.* v. *Association of Wash. Stevedoring Cos.*, 435 U. S. 734 (1978). The Court of Federal Claims noted that this Court has never overruled *Thames & Mersey* and ruled that application of § 4371 to policies insuring goods in export transit violates the Export Clause. 31 Fed. Cl. 500 (1994). The Court of Appeals for the Federal Circuit affirmed. 59 F. 3d 1234 (1995). We agreed to hear this case to decide whether we should overrule *Thames & Mersey*. 516 U.S. __ (1995).

II

The Export Clause states simply and directly: "No Tax or Duty shall be laid on Articles exported from any State." U.S. Const., Art. I, § 9, cl. 5. We have had few occasions to interpret the lan-

[1] The tax does not apply if a policy issued by a foreign insurer is "signed or countersigned by an officer or agent of the insurer in a State, or in the District of Columbia, within which such insurer is authorized to do business." 26 U. S. C. § 4373(1) (1982 ed.).

guage of the Export Clause, but our cases have broadly exempted from federal taxation not only export goods, but also services and activities closely related to the export process. At the same time, we have attempted to limit the term "Articles exported" to permit federal taxation of pre-export goods and services.

Our early cases upheld federal assessments on the manufacture of particular products ultimately intended for export by finding that pre-export products are not "Articles exported." See *Pace* v. *Burgess*, 92 U. S. 372 (1876); *Turpin* v. *Burgess*, 117 U. S. 504 (1886); *Cornell* v. *Coyne*, 192 U. S. 418 (1904). *Pace* and *Turpin* both involved a federal excise tax on tobacco products. In *Pace*, though tobacco intended for export was exempted from the tax, the exemption itself was subject to a per-package stamp charge of 25 cents. When a tobacco manufacturer challenged the stamp charge, we upheld the charge on the basis that the stamps were designed to prevent fraud in the export exemption from the excise tax and did not, therefore, represent a tax on exports. 92 U.S., at 375. When Congress later repealed the 25-cent charge for the exemption stamp in a statute that referred to the stamp as an "export tax," another manufacturer sued to recover the money it had paid for the exemption stamps. See *Turpin, supra*. Without disturbing the prior ruling in *Pace* that the stamp charge was not a tax on exports, 117 U.S., at 505, we explained that the prohibition of the Export Clause "has reference to the imposition of duties on goods by reason or because of their exportation or intended exportation, or whilst they are being exported," *id.*, at 507. We said that the plaintiffs would have had no Export Clause claim even if there had been no exemption from the excise because the goods were not in the course of exportation and might never be exported. *Ibid. Turpin* broadly suggested that the Export Clause prohibits both taxes levied on goods in the course of exportation and taxes directed specifically at exports.

In *Cornell*, the Court addressed whether the Export Clause prohibited application of a federal excise tax on filled cheese manufactured under contract for export. Looking to the analysis set out in *Turpin*, we rejected the contention that the Export Clause bars application of a nondiscriminatory tax imposed before the product entered the course of exportation. "The true construction of the constitutional provision is that no burden by way of tax or duty can be cast upon the exportation of articles, and does not mean that articles exported are relieved from the prior ordinary burdens of taxation which rest upon all property similarly situated." *Cornell, supra*, at 427. *Pace, Turpin*, and *Cornell* made clear that nondiscriminatory pre-exportation assessments do not violate the Export Clause, even if the goods are eventually exported.

At the same time we were defining a domain within which nondiscriminatory taxes could permissibly be imposed on goods intended for export, we were also making clear that the Export Clause strictly prohibits any tax or duty, discriminatory or not, that falls on exports during the course of exportation. See *Fairbank* v. *United States*, 181 U. S. 283 (1901); *United States* v. *Hvoslef*, 237 U. S. 1 (1915); *Thames & Mersey Marine Ins. Co.* v. *United States, supra.* In *Fairbank*, for example, we addressed a federal stamp tax on bills of lading for export shipments imposed by the War Revenue Act of 1898. The Court found that the tax was facially discriminatory, *Fairbank, supra,* at 290, and, though not directly imposed on the goods being exported, the tax was nevertheless "in effect a duty on the article transported," 181 U. S., at 294. Consequently, the tax fell directly into the category of forbidden taxes on exports defined in *Turpin*. In striking down the tax, we said:

> "The requirement of the Constitution is that exports should be free from any governmental burden. The language is 'no tax or duty.' Whether such provision is or is not wise is a question of policy with which the courts have nothing to do. We know historically that it was one of the compromises which entered into and made possible the adoption of the Constitution. It is a restriction on the power of Congress . . . ." 181 U. S., at 290.

Hvoslef and *Thames & Mersey* differed from *Fairbank* in that the taxes imposed in those cases—on ship charters and marine insurance, respectively—did not facially discriminate against exports. The Court nonetheless prohibited the application of those generally applicable, nondiscriminatory taxes to the transactions at issue because each tax was, in effect, a tax on exports. The type of charter contract at issue in *Hvoslef* was "in contemplation of law a mere contract of affreightment," 237 U.S., at 16, and we found that the tax, as applied to charters for exportation, "was in substance a tax on the exportation; and a tax on the exportation is a tax on the exports," *id.*, at 17. Likewise, in *Thames & Mersey*, we found that "proper insurance during the voyage is one of the necessities of exportation" and that "the taxation of policies insuring cargoes during their transit to foreign ports is as much a burden on exporting as if it were laid on the charter parties, the bills of lading, or the goods themselves." 237 U. S., at 27.

Shortly after *Hvoslef* and *Thames & Mersey*, the Court rejected an attempt to shield from taxation the net income of a company engaged in the export business. *William E. Peck & Co.* v. *Lowe*, 247 U. S. 165 (1918). In accordance with the analysis set out in *Turpin*, we found both that the tax was nondiscriminatory and that "[i]t is not laid on articles in course of exportation or on anything which inherently or by the usages of commerce is embraced in exportation or any of its processes." 247 U. S., at 174.

Only a few years later the Court struck down the application of a tax on the export sale of certain baseball equipment. See *A. G. Spalding & Bros.* v. *Edwards*, 262 U. S. 66 (1923). Although the tax was clearly nondiscriminatory, we explained that the goods being taxed had entered the course of exportation when they were delivered to the export carrier. *Id.*, at 70. Because the taxable event, the transfer of title, occurred at the same moment the goods entered the course of exportation, we held that the tax could not constitutionally be applied to the export sale. *Id.*, at 69–70.

The Court has strictly enforced the Export Clause's prohibition against federal taxation of goods in export transit, and we have extended that protection to certain services and activities closely related to the export process. We have not, however, exempted pre-export goods and services from ordinary tax burdens; nor have we exempted from federal taxation various services and activities only tangentially related to the export process.

III

The Government concedes, as it did below, that this case is largely indistinguishable from *Thames & Mersey* and that, if *Thames & Mersey* is still good law, the tax assessed against IBM under § 4371 violates the Export Clause. See

Tr. of Oral Arg. 5; 59 F. 3d, at 1237. The parties apparently agree that there is no legally significant distinction between the insurance policies at issue in this case and those at issue in *Thames & Mersey*, and, accordingly, the Government asks that we overrule *Thames & Mersey.*

The Government asserts that the Export Clause permits the imposition of generally applicable, nondiscriminatory taxes, even on goods in export transit. The Government urges that we have historically interpreted the Commerce, Import-Export, and Export Clauses in harmony and that we have rejected the theory underlying *Thames & Mersey* in the context of the Commerce and Import-Export Clauses. Accordingly, the Government contends that our Export Clause jurisprudence, symbolized by *Thames & Mersey*, has become an anachronism in need of modernization. The Government asks us to reinterpret the Export Clause to permit the imposition of generally applicable, nondiscriminatory taxes as we have under the Commerce Clause and, it argues, under the Import-Export Clause.

A

The Government contends that our dormant Commerce Clause jurisprudence has shifted dramatically and that our traditional understanding of the Export Clause, which is based partly on an outmoded view of the Commerce Clause, can no longer be justified. It is true that some of our early Export Clause cases relied on an interpretation of the Commerce Clause that we have since rejected. In *Fairbank*, 181 U. S., at 298–300, for example, we analogized to *Robbins* v. *Shelby County Taxing Dist.*, 120 U. S. 489, 497 (1887), in which we held that "[i]nterstate commerce cannot be taxed at all [by the States], even though the same amount of tax should be laid on domestic commerce, or that which is carried on solely within the state." Referring to the categorical ban on taxation of interstate commerce declared in *Robbins*, we likened the scope of the Commerce Clause's ban on state taxation of interstate commerce to the Export Clause's ban on federal taxation of exports. *Fairbank, supra*, at 300; see also *Hvoslef*, 237 U. S., at 15 ("The court [in *Fairbank*] found an analogy in the construction which had been given to the commerce clause in protecting interstate commerce from state legislation imposing direct burdens"). After *Thames & Mersey*, the Commerce Clause construction espoused in *Robbins* fell out of favor, see *Western Live Stock* v. *Bureau of Revenue*, 303 U. S. 250, 254 (1938) ("It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing the business"), and we expressly disavowed that view in *Complete Auto Transit, Inc.* v. *Brady*, 430 U. S. 274, 288—289 (1977).

Our rejection in *Complete Auto* of much of our early dormant Commerce Clause jurisprudence did not, however, signal a similar rejection of our Export Clause cases. Our decades-long struggle over the meaning of the nontextual negative command of the dormant Commerce Clause does not lead to the conclusion that our interpretation of the textual command of the Export Clause is equally fluid. At one time, the Court may have thought that the dormant Commerce Clause required a strict ban on state taxation of interstate commerce, but the text did not require that view.[2] The text of the Export Clause, on the other hand, expressly prohibits Congress from laying any tax or duty on exports. These textual disparities strongly suggest that shifts in the Court's view of the scope of the dormant Commerce Clause should not, and indeed cannot, govern our interpretation of the Export Clause. Cf. *Richfield Oil Corp.* v. *State Bd. of Equalization*, 329 U. S. 69, 75–76 (1946) (distinguishing accommodations made under the Commerce Clause from the express textual prohibition of the Import-Export Clause).

B

The Government's primary assertion is that modifications in our Import-Export Clause jurisprudence require parallel modifications in the Export Clause context. More specifically, the Government argues that our decisions in *Michelin Tire Corp.* v. *Wages*, 423 U. S. 276 (1976), and *Department of Revenue of Wash.* v. *Association of Wash. Stevedoring Cos.*, 435 U. S. 734 (1978), establish that States may impose generally applicable, nondiscriminatory taxes even if those taxes fall on imports or exports. The Export Clause, the Government contends, is no more restrictive.

The Import-Export Clause, which is textually similar to the Export Clause, says in relevant part, "No State shall . . . lay any Imposts or Duties on Imports or Exports." U. S. Const., Art. I, § 10, cl. 2. Though minor textual differences exist and the Clauses are directed at different sovereigns, historically both have been treated as broad bans on taxation of exports, and in several cases the Court has interpreted the provisions of the two Clauses in tandem. For instance, in the Court's first decision interpreting the Import-Export Clause, Chief Justice Marshall said:

> "The States are forbidden to lay a duty on exports, and the United States are forbidden to lay a tax or duty on articles exported from any State. There is some diversity in language, but none is perceivable in the act which is prohibited." *Brown* v. *Maryland*, 12 Wheat. 419, 445 (1827).

See also *Kosydar* v. *National Cash Register Co.*, 417 U. S. 62, 67, n. 5 (1974); *Hvoslef, supra,* at 13–14; *Cornell*, 192 U. S., at 427–428; *Turpin*, 117 U. S., at 506–507. The Government argues that our longstanding parallel interpretations of the two Clauses require judgment in its favor. We disagree.

In *Michelin*, we addressed whether a State could impose a nondiscriminatory ad valorem property tax on imported goods that were no longer in import transit. Michelin, which imported tires from Canada and France and stored them in a warehouse, argued that Georgia could not constitutionally assess ad valorem property taxes against its imported tires. We explained that "[t]he Framers of the Constitution . . . sought to alleviate three main concerns": (i) ensuring that the Federal Government speaks with one voice when regulating foreign commerce; (ii) preserving import revenues as a major source of federal revenue; and (iii) preventing disharmony likely to be caused if seaboard States taxed goods coming through their ports. *Michelin, supra*, at 285–286. The Court found that nondiscriminatory ad valorem taxes violate none of these policies. A century earlier, however, the Court had ruled that, under the "original package doctrine," a State could not impose such a tax until the goods had lost their

[2] The Commerce Clause is an express grant of power to Congress to "regulate Commerce . . . among the several States." U. S. Const., Art. I, § 8, cl. 3. It does not expressly prohibit the States from doing anything, though we have long recognized negative implications of the Clause that prevent certain state taxation even when Congress has failed to legislate. See *Fulton Corp.* v. *Faulkner*, 516 U. S. __, __ (1996) (slip op., at 4–5); *Quill Corp.* v. *North Dakota*, 504 U. S. 298, 309 (1992).

character as imports and had been incorporated into the mass of property in the State. *Low* v. *Austin*, 13 Wall. 29, 34 (1872). The *Michelin* Court overruled *Low* and held that the nondiscriminatory property tax levied on Michelin's inventory of imported tires did not violate the Import-Export Clause because it was not an impost or duty on imports. 423 U. S., at 301. See also *Limbach* v. *Hooven & Allison Co.*, 466 U. S. 353 (1984) (reaffirming that *Michelin* expressly overruled the original package doctrine altogether and not merely *Low* on its facts).

Two years later, in *Washington Stevedoring*, we upheld against an Import-Export Clause challenge a nondiscriminatory state tax assessed against the compensation received by stevedoring companies for services performed within the State. The Court found that Washington's stevedoring tax did not violate the policies underlying the Import-Export Clause. Unlike the property tax at issue in *Michelin*, the activity taxed by Washington occurred while imports and exports were in transit. That fact was not dispositive, however, because the tax did not fall on the goods themselves:

> "The levy reaches only the business of loading and unloading ships or, in other words, the business of transporting cargo within the State of Washington. Despite the existence of the first distinction, the presence of the second leads to the conclusion that the Washington tax is not a prohibited 'Impost or Duty' when it violates none of the policies [that animate the Import-Export Clause]." *Washington Stevedoring, supra*, at 755.

Relying on *Canton R. Co.* v. *Rogan*, 340 U. S. 511 (1951), which upheld a tax on the gross receipts of a railroad that operated a marine terminal and transported imports and exports, we ruled in *Washington Stevedoring* that taxation of transportation services, whether by railroad on the docks or by stevedores loading and unloading ships, did not relate to the value of the goods and could not be considered imposts or duties on the goods themselves. 435 U.S., at 757.

1

A tax on policies insuring exports is not, precisely speaking, the same as a tax on exports, but *Thames & Mersey* held that they were functionally the same under the Export Clause. We noted in *Washington Stevedoring* that one may question the finding in *Thames & Mersey* that the tax was essentially a tax upon the exportation itself. 435 U. S., at 756, n. 21. We expressed concern that "[t]he basis for distinguishing *Thames & Mersey* is less clear" than for *Fairbank* or *Richfield Oil*, because the marine insurance policies in *Thames & Mersey* arguably "had a value apart from the value of the goods." 435 U. S., at 756, n. 21. Nevertheless, the Government apparently has chosen not to challenge that aspect of *Thames & Mersey* in this case. Tr. of Oral Arg. 5, 8–9, 40. When questioned on that implicit concession at oral argument, the Government admitted that it "chose not to" argue that § 4371 does not impose a tax on the goods themselves. *Id.*, at 9. It would be inappropriate for us to reexamine in this case, without the benefit of the parties' briefing, whether the policies on which § 4371 is assessed are so closely connected to the goods that the tax is, in essence, a tax on exports.[3] See, *e.g., id.*, at 27–28 ("[T]he record doesn't reveal the sort of statistical information Justice Breyer was suggesting might be relevant" to determine "whether this is sufficiently indirect that it's not a tax on exports, . . . because the Government has conceded throughout that they are not disputing that this tax, if discriminatory, is in violation of the Constitution").

Stare decisis is a "principle of policy," *Helvering* v. *Hallock*, 309 U. S. 106, 119 (1940), and not "an inexorable command," *Payne* v. *Tennessee*, 501 U. S. 808, 828 (1991). Applying that policy, we frequently have declined to overrule cases in appropriate circumstances because *stare decisis* "promotes the evenhanded, predictable, and consistent development of legal principles, fosters reliance on judicial decisions, and contributes to the actual and perceived integrity of the judicial process." *Id.*, at 827. "[E]ven in constitutional cases, the doctrine carries such persuasive force that we have always required a departure from precedent to be supported by some 'special justification.'" *Id.*, at 842 (SOUTER, J., concurring) (quoting *Arizona* v. *Rumsey*, 467 U. S. 203, 212 (1984)).

Though from time to time we have overruled governing decisions that are "unworkable or are badly reasoned," *Payne, supra*, at 827; see *Smith* v. *Allwright*, 321 U. S. 649, 665 (1944), we have rarely done so on grounds not advanced by the parties. *Thames & Mersey* has been controlling precedent for over 80 years, and the Government does not, indeed could not, argue that the rule established there is "unworkable." Despite the dissent's speculative protestations to the contrary, *post*, at 9–11, there is simply no evidence that *Thames & Mersey* has caused or will cause uncertainty in commercial export transactions. The principles that animate our policy of *stare decisis* caution against overruling a long-standing precedent on a theory not argued by the parties, and we decline to do so in this case.[4]

2

What the Government does argue is that our Import-Export Clause cases require us to overrule *Thames & Mersey*[5]. We have good reason to hesitate before adopting the analysis of our recent Import-Export Clause cases into our Export Clause jurisprudence. Though we have frequently interpreted the Clauses together, see *supra*, at 9–10, our more

[3] The Court has never held that the Export Clause prohibits only direct taxation of goods in export transit. In *Brown* v. *Maryland*, 12 Wheat. 419 (1827), Chief Justice Marshall expressed in dicta his skepticism that a federal occupational tax on exporters could pass scrutiny under the Export Clause. *Id.*, at 445 ("[W]ould government be permitted to shield itself from the just censure to which this attempt to evade the prohibitions of the constitution would expose it, by saying that this was a tax on the person, not on the article, and that the legislature had a right to tax occupations?"). In *Fairbank, Hvoslef*, and *Thames & Mersey*, we struck down taxes that were not assessed directly on goods in export transit, but which the Court found to be so closely related as to be effectively a tax on the goods themselves. We have never repudiated that principle, but neither have we ever carefully defined how we decide whether a particular federal tax is sufficiently related to the goods or their value to violate the Export Clause. To the extent the issue was raised in the petition for certiorari, the Government failed to address the issue in its brief on the merits and therefore has abandoned it. See *Posters 'N' Things, Ltd.* v. *United States*, 511 U. S. ___, ___ (1994) (slip op., at 15); *Russell* v. *United States*, 369 U. S. 749, 754, n. 7 (1962).

[4] The dissent suggests that "the Court assumes the statute to be invalid rather than deciding it to be so." *Post*, at 2. We make no such assumptions. Rather, we begin with a longstanding decision that, by all accounts, controls this case. Even the Government agrees that Congress enacted a law whose application in this case directly contravenes our holding in *Thames & Mersey*. We sit not to condemn § 4371, but rather to determine whether it is to be saved by overruling binding precedent.

[5] The dissent suggests that we make a "serious mistake" in deciding whether a nondiscriminatory tax on goods violates the Export Clause, *post*, at 19. We do not agree that it is a mistake to address the arguments actually advanced by the parties.

recent Import-Export Clause cases, on which the Government relies, caution that meaningful textual differences exist and should not be overlooked. The Export Clause prohibits Congress from laying any "Tax or Duty" on exports, while the Import-Export Clause prevents the States from laying any "Imposts or Duties" on imports or exports. In both *Michelin* and *Washington Stevedoring*, we left open the possibility that a particular state assessment might not properly be called an impost or duty, and thus would be beyond the reach of the Import-Export Clause, while an identical federal assessment might properly be called a tax and would be subject to the Export Clause. Though we found in *Michelin* that a nondiscriminatory state property tax does not transgress the policy dictates of the Import-Export Clause, we also recognized that the Import-Export Clause is "not written in terms of a broad prohibition of every 'tax,'" and that impost and duty are narrower terms than tax. 423 U. S., at 290–293. In *Washington Stevedoring*, we likewise rejected the assertion that the Import-Export Clause absolutely prohibits all taxation of imports and exports. 435 U. S., at 759. We said that "the term 'Impost or Duty' is not self-defining and does not necessarily encompass all taxes" and that the respondents' argument to the contrary ignored "the central holding of *Michelin* that the absolute ban is only of 'Imposts or Duties' and not of all taxes." *Ibid.*

The distinction between imposts or duties and taxes is especially pertinent in light of the peculiar definitional analysis we chose in *Michelin*. Finding substantial ambiguity in the phrase "Imposts or Duties," we "decline[d] to presume it was intended to embrace taxation that does not create the evils the Clause was specifically intended to eliminate." *Michelin, supra*, at 293–294. We entirely bypassed the etymological inquiry into the proper meaning of the terms "impost" and "duty," and instead created a regime in which those terms are conclusions to be drawn from an examination into whether a particular assessment "was the type of exaction that was regarded as objectionable by the Framers of the Constitution." 423 U. S., at 286. We are not prepared to say that the word "Tax" is "sufficiently ambiguous," *id.*, at 293, that we may ignore its common, and usually expansive,[6] meaning in favor of an Export Clause decisional rule in which a tax is not a "Tax" unless it discriminates against exports. Consequently, *Michelin* and *Washington Stevedoring*, which held that the assessments in question were not "Imposts or Duties" at all, do not logically validate the assessment at issue in this case, which, by all accounts, remains a "Tax."

It is not intuitively obvious that *Michelin*'s three-pronged analysis of the Framers' concerns is really just another way of stating a nondiscrimination principle. But even if it were, the Government cannot reasonably rely on *Michelin* to govern the Export Clause because *Michelin* drew its analysis around the phrase "Imposts or Duties" and expressly excluded the broader term "Tax" that appears in the Export Clause. *Michelin* marked a more permissive approach to state taxation under the Import-Export Clause only by distinguishing the presumptively stricter language of the Export Clause. We agree with the Government that *Michelin* informs our decision in this case, but not in a way that supports the Government's position. It is simply no longer true that the Court perceives no substantive difference between the two Clauses.

We are similarly hesitant to adopt the Import-Export Clause's policy-based analysis without some indication that the Export Clause was intended to alleviate the same "evils" to which the Import-Export Clause was directed. Unlike the Import-Export Clause, which was intended to protect federal supremacy in international commerce, to preserve federal revenue from import duties and imposts, and to prevent coastal States with ports from taking unfair advantage of inland States, see *Michelin, supra*, at 285–286, the Export Clause serves none of those goals. Indeed, textually, the Export Clause does quite the opposite. It specifically prohibits Congress from regulating international commerce through export taxes, disallows any attempt to raise federal revenue from exports, and has no direct effect on the way the States treat imports and exports.

As a purely historical matter, the Export Clause was originally proposed by delegates to the Federal Convention from the Southern States, who feared that the Northern States would control Congress and would use taxes and duties on exports to raise a disproportionate share of federal revenues from the South. See 2 M. Farrand, The Records of the Federal Convention of 1787, pp. 95, 305–308, 359–363 (rev. ed. 1966). The Government argues that this "narrow historical purpose" justifies a narrow interpretation of the text and that application of § 4371 to policies insuring exports does not conflict with the policies embodied in the Clause. Brief for United States 32–34. While the original impetus may have had a narrow focus, the remedial provision that ultimately became the Export Clause does not, and there is substantial evidence from the Debates that proponents of the Clause fully intended the breadth of scope that is evident in the language. See, *e. g.*, 2 Farrand, Records of the Federal Convention, at 220 (Mr. King: "In two great points the hands of the Legislature were absolutely tied. The importation of slaves could not be prohibited—exports could not be taxed"); *id.*, at 305 ("Mr. Mason urged the necessity of connecting with the power of levying taxes . . . that no tax should be laid on exports"); *id.*, at 360 (Mr. Elseworth [sic]: "There are solid reasons agst. Congs taxing exports"); *ibid.* ("Mr. Butler was strenuously opposed to a power over exports"); *id.*, at 361 (Mr. Sherman: "It is best to prohibit the National legislature in all cases"); *id.*, at 362 ("Mr. Gerry was strenuously opposed to the power over exports").

The Government argued for a different narrow interpretation of the Export Clause in *Fairbank*. See 181 U. S., at 292–293. Arguing that the Debates expressed a primary interest in diffusing sectional conflicts, the Government urged the *Fairbank* Court to interpret the Export Clause to permit taxation of "the act of exportation or the document evidencing the receipt of goods for export, for these exist with substantial uniformity throughout the country." *Id.*, at 292. We rejected that argument:

> "If mere discrimination between the States was all that was contemplated, it would seem to follow that an *ad valorem* tax upon all exports would not be obnoxious to this constitutional prohibition. But surely under this limitation Congress can impose an export tax neither on one article of export, nor on all articles of export." *Ibid.*

[6] Though *Michelin* discusses "taxes" in terms of "every exaction," 423 U. S., at 290, it also suggests that at the time of the Founding "probably only capitation, land, and general property exactions were known by the term 'tax' rather than the term 'duty,'" *id.*, at 291. In any event, the *Michelin* Court understood that the terms used in the Export Clause were broader than those used in the Import-Export Clause.

As in *Fairbank*, we think the text of the constitutional provision provides a better decisional guide than that offered by the Government. The Government's policy argument—that the Framers intended the Export Clause to narrowly alleviate the fear of northern repression through taxation of southern exports by prohibiting only discriminatory taxes—cannot be squared with the broad language of the Clause. The better reading, that adopted by our earlier cases, is that the Framers sought to alleviate their concerns by completely denying to Congress the power to tax exports at all.

3

Even assuming that *Michelin* and *Washington Stevedoring* govern our Export Clause inquiry in this case, the Government's argument falls short of its goal. Our holdings in *Michelin* and *Washington Stevedoring* do not reach the facts of this case and, more importantly, do not interpret the Import-Export Clause to permit assessment of nondiscriminatory taxes on imports and exports in transit. *Michelin* involved a tax on goods, but the goods were no longer in transit. The tax in *Washington Stevedoring* burdened imports and exports while they were still in transit, but it did not fall directly on the goods themselves. This case, as it comes to us, is a hybrid in which the tax both burdens exports during transit and—as the Government concedes and our earlier cases held—is essentially a tax on the goods themselves. The Government argues that *Michelin* and *Washington Stevedoring* by analogy permit Congress to impose generally applicable, nondiscriminatory taxes that fall directly on exports in transit. Brief for United States 32 (*Michelin* and *Washington Stevedoring* ''demonstrate that, when a generally applicable, nondiscriminatory tax is at issue, the mere fact that the tax applies also to goods that are in the export or import process does not provide a constitutional immunity from taxation''). If this contention is to succeed, the Government at the very least must show that our Import-Export Clause jurisprudence now permits a State to impose a nondiscriminatory tax directly on goods in import or export transit. We think the Government has failed to make that showing.

The Court has never upheld a state tax assessed directly on goods in import or export transit. In *Michelin*, we suggested that the Import-Export Clause would invalidate application of a nondiscriminatory property tax to goods still in import or export transit. 423 U. S., at 290 (compliance with the Import-Export Clause may be secured ''by prohibiting the assessment of even nondiscriminatory property taxes on [import or export] goods which are merely in transit through the State when the tax is assessed''). See also *Virginia Indonesia Co.* v. *Harris County Appraisal Dist.*, 910 S. W. 2d 905, 915 (Tex. 1995) (invalidating application of a nondiscriminatory ad valorem property tax to goods in export transit).

We also declined to endorse the Government's theory in *Washington Stevedoring*. After reciting that the Court in *Canton R. Co.* had distinguished *Thames & Mersey, Fairbank*, and *Richfield Oil*, we pointed out that in those cases ''the State [or Federal Government] had taxed either the goods or activity so connected with the goods that the levy amounted to a tax on the goods themselves.'' *Washington Stevedoring*, 435 U. S., at 756, n. 21. We expressly declined to ''reach the question of the applicability of the *Michelin* approach when a State directly taxes imports or exports in transit,'' *id.*, at 757, n. 23, because, although the goods in that case were in transit, the tax fell on ''a service distinct from the goods and their value,'' *id.*, at 757. Thus, contrary to the Government's contention, this Court's Import-Export Clause cases have not upheld the validity of generally applicable, nondiscriminatory taxes that fall on imports or exports in transit. We think those cases leave us free to follow the express textual command of the Export Clause to prohibit the application of any tax ''laid on Articles exported from any State.''

* * * * *

We conclude that the Export Clause does not permit assessment of nondiscriminatory federal taxes on goods in export transit. Reexamination of the question whether a particular assessment on an activity or service is so closely connected to the goods as to amount to a tax on the goods themselves must await another day. We decline to overrule *Thames & Mersey*. The judgment of the Court of Appeals for the Federal Circuit is affirmed.

It is so ordered.

Section 6323.—Validity and Priority Against Certain Persons

Ct.D. 2059

SUPREME COURT OF THE UNITED STATES

No. 95–323

UNITED STATES, PETITIONER v. THOMAS R. NOLAND, TRUSTEE FOR DEBTOR FIRST TRUCK LINES, INC.

517 U.S.—

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

May 13, 1996

Syllabus

The Internal Revenue Service filed claims in the Bankruptcy Court for taxes, interest, and penalties that accrued after debtor First Truck Lines, Inc., sought relief under Chapter 11 of the Bankruptcy Code but before the case was converted to a Chapter 7 bankruptcy. The court found that all of the IRS's claims were entitled to first priority as administrative expenses under 11 U. S. C. §§ 503(b)(1)(C) and 507(a)(1), but held that the penalty claim was subject to ''equitable subordination'' under § 510(c), which the court interpreted as giving it authority not only to deal with inequitable Government conduct, but also to adjust a statutory priority of a category of claims. The court's decision to subordinate the penalty claim to the claims of the general unsecured creditors was affirmed by the District Court and the Sixth Circuit, which concluded that postpetition, nonpecuniary loss tax penalty claims are susceptible to subordination by their very nature.

Held: A bankruptcy court may not equitably subordinate claims on a categorical basis in derogation of Congress's priorities scheme. The language of § 510(c), principles of statutory construction, and legislative history clearly indicate Congress's intent in its 1978 revision of the Code to use the existing judge-made doctrine of equitable subordination as the starting point for deciding when subordination is appropriate. By adopting ''principles of equitable subordination,'' § 510(c) allows a bankruptcy court to reorder a tax penalty when justified by particular facts. It is also clear that Congress meant to give courts some leeway to develop the doctrine. However, a reading of the statute that would give courts leeway broad enough to allow subordination at odds with the congressional ordering of priorities by category is improbable in the extreme. The statute would then empower a court to modify the priority provision's operation at the same level at which Congress operated when it made its characteristically general judgment to establish the hierarchy of claims in the first place, thus delegating legislative revision, not authorizing equitable exception. Nonetheless, just such a legislative type of decision underlies the reordering of priorities here. The Sixth Circuit's decision runs directly counter to Congress's policy judgment that a postpetition tax penalty should receive the priority of an administrative expense. Since the Sixth Circuit's rationale was inappropriately categorical

in nature, this Court need not decide whether a bankruptcy court must always find creditor misconduct before a claim may be equitably subordinated.

48 F. 3d 210, reversed and remanded.

SOUTER, J., delivered the opinion for a unanimous Court.

JUSTICE SOUTER delivered the opinion of the Court.

The issue in this case is the scope of a bankruptcy court's power of equitable subordination under 11 U.S.C. § 510(c). Here, in the absence of any finding of inequitable conduct on the part of the Government, the Bankruptcy Court subordinated the Government's claim for a postpetition, noncompensatory tax penalty, which would normally receive first priority in bankruptcy as an "administrative expense," §§ 503(b)(1)(C), 507(a)(1). We hold that the bankruptcy court may not equitably subordinate claims on a categorical basis in derogation of Congress's scheme of priorities.

In April 1986, First Truck Lines, Inc., voluntarily filed for relief under Chapter 11 of the Bankruptcy Code, and in the subsequent operation of its business as a debtor-in-possession incurred, but failed to discharge, tax liabilities to the Internal Revenue Service. First Truck moved to convert the case to a Chapter 7 liquidation in June 1988, and in August 1988 the Bankruptcy Court granted that motion and appointed respondent Thomas R. Noland as trustee. The liquidation of the estate's assets raised insufficient funds to pay all of the creditors.

After the conversion, the IRS filed claims for taxes, interest, and penalties that accrued after the Chapter 11 filing but before the Chapter 7 conversion, and although the parties agreed that the claims for taxes and interest were entitled to priority as administrative expenses, §§ 503(b), 507(a)(1), and 726(a)(1),[1] they disagreed about the priority to be given tax penalties. The Bankruptcy Court determined that the penalties (like the taxes and interest) were administrative expenses under § 503(b) but held them to be subject to equitable subordination under § 510(c).[2] In so doing, the Court read that section to provide authority not only to deal with inequitable conduct on the Government's part, but also to adjust a statutory priority of a category of claims. The Bankruptcy Court accordingly weighed the relative equities that seemed to flow from what it described as "the Code's preference for compensating actual loss claims," and subordinated the tax penalty claim to those of the general unsecured creditors. *In re First Truck Lines, Inc.*, 141 B. R. 621, 629 (SD Ohio 1992). The District Court affirmed. *Internal Revenue Service* v. *Noland, 190 B. R. 827 (SD Ohio 1993).*

After reviewing the legislative history of the 1978 revision to the Bankruptcy Code and several recent appeals cases on equitable subordination of tax penalties, the Sixth Circuit affirmed, as well. *In re First Truck Lines, Inc.*, 48 F. 3d 210 (1995). The Sixth Circuit stated that it did

> "not see the fairness or the justice in permitting the Commissioner's claim for tax penalties, which are not being assessed because of pecuniary losses to the Internal Revenue Service, to enjoy an equal or higher priority with claims based on the extension of value to the debtor, whether secured or not. Further, assessing tax penalties against the estate of a debtor no longer in existence serves no punitive purpose. Because of the nature of postpetition, nonpecuniary loss tax penalty claims in a Chapter 7 case, we believe such claims are susceptible to subordination. To hold otherwise would be to allow creditors who have supported the business during its attempt to reorganize to be penalized once that effort has failed and there is not enough to go around." *Id.*, at 218.

See also *Burden* v. *United States*, 917 F. 2d 115, 120 (CA3 1990); *Schultz Broadway Inn* v. *United States*, 912 F. 2d 230, 234 (CA8 1990); *In re Virtual Network Services Corp.*, 902 F. 2d 1246, 1250 (CA7 1990). We granted certiorari to determine the appropriate scope of the power under the Bankruptcy Code to subordinate a tax penalty, 516 U. S. ___ (1995), and we now reverse.

The judge-made doctrine of equitable subordination predates Congress's revision of the Code in 1978. Relying in part on our earlier cases, see, *e.g., Comstock* v. Group of Institutional Investors, 335 U. S. 211 (1948); *Pepper* v. *Litton*, 308 U. S. 295 (1939); *Taylor* v. *Standard Gas & Elec. Co.*, 306 U. S. 307 (1939), the Fifth Circuit, in its influential opinion in *In re Mobile Steel Co.*, 563 F. 2d 692, 700 (CA5 1977), observed that the application of the doctrine was generally triggered by a showing that the creditor had engaged in "some type of inequitable conduct." *Mobile Steel* discussed two further conditions relating to the application of the doctrine: that the misconduct have "resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant," and that the subordination "not be inconsistent with the provisions of the Bankruptcy Act." *Ibid*. This last requirement has been read as a "reminder to the bankruptcy court that although it is a court of equity, it is not free to adjust the legally valid claim of an innocent party who asserts the claim in good faith merely because the court perceives that the result is inequitable." DeNatale & Abram, The Doctrine of Equitable Subordination as Applied to Nonmanagement Creditors, 40 Bus. Law. 417, 428 (1985). The district courts and courts of appeals have generally followed the *Mobile Steel* formulation, *In re Baker & Getty Financial Services, Inc.*, 974 F. 2d 712, 717 (CA6 1992).

Although Congress included no explicit criteria for equitable subordination when it enacted § 510(c)(1), the reference in § 510(c) to "principles of equitable subordination," clearly indicates congressional intent at least to start with existing doctrine. This conclusion is confirmed both by principles of statutory construction, see *Midlantic Nat. Bank* v. *New Jersey Dept. of Environmental Protection*, 474 U. S. 494, 501 (1986) ("The normal rule of statutory construction is that if Congress intends for legislation to change the interpretation of a judicially created concept, it makes that intent specific. The Court has followed this rule with particular care in construing the scope of bankruptcy codifications") (citation omitted), and by statements in the legislative history that Congress "intended that the term 'principles of equitable subordination' follow existing case law and leave to the courts development of this principle," 124 Cong. Rec. 32398 (1978)

[1] Section 507(a)(1) provides, in relevant part: "(a) The following expenses and claims have priority in the following order: (1) First, administrative expenses allowed under section 503(b) of this title . . . ." Under § 503(b)(1), administrative expenses include "any tax . . . incurred by the estate" (with certain exceptions not relevant here), as well as "any fine [or] penalty . . . relating to [such] a tax . . . ." Section 726(a)(1) adopts the order of payment specified in § 507 for Chapter 7 proceedings.

[2] Section 510(c) provides that "the court may . . . under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim . . . ."

(Rep. Edwards); see also *id.*, at 33998 (Sen. DeConcini). In keeping with pre-1978 doctrine, many Courts of Appeals have continued to require inequitable conduct before allowing the equitable subordination of most claims, see, *e.g., In re Fabricators, Inc.*, 926 F. 2d 1458, 1464 (CA5 1991); *In re Bellanca Aircraft Corp.*, 850 F. 2d 1275, 1282–1283 (CA8 1988), although several have done away with the requirement when the claim in question was a tax penalty. See, *e.g., Burden, supra*, at 120; *Schultz, supra*, at 234; *In re Virtual Network, supra,* at 1250.

Section 510(c) may of course be applied to subordinate a tax penalty, since the Code's requirement that a Chapter 7 trustee must distribute assets "in the order specified in . . . section 507," (which gives a first priority to administrative expense tax penalties) is subject to the qualification, "[e]xcept as provided in section 510 of this title . . . ." 11 U.S.C. § 726(a). Thus, "principles of equitable subordination" may allow a bankruptcy court to reorder a tax penalty in a given case. It is almost as clear that Congress meant to give courts some leeway to develop the doctrine, 124 Cong. Rec. 33998 (1978), rather than to freeze the pre-1978 law in place. The question is whether that leeway is broad enough to allow subordination at odds with the congressional ordering of priorities by category.

The answer turns on Congress's probable intent to preserve the distinction between the relative levels of generality at which trial courts and legislatures respectively function in the normal course. Hence, the adoption in § 510(c) of "principles of equitable subordination" permits a court to make exceptions to a general rule when justified by particular facts, cf. *Hecht Co.* v. *Bowles*, 321 U. S. 321, 329 (1944) ("The essence of equity jurisdiction has been the power of the Chancellor to do equity and to mould each decree to the necessities of the particular case"). But if the provision also authorized a court to conclude on a general, categorical level that tax penalties should not be treated as administrative expenses to be paid first, it would empower a court to modify the operation of the priority statute at the same level at which Congress operated when it made its characteristically general judgment to establish the hierarchy of claims in the first place. That is, the distinction between characteristic legislative and trial court functions would simply be swept away, and the statute would delegate legislative revision, not authorize equitable exception. We find such a reading improbable in the extreme. "Decisions about the treatment of categories of claims in bankruptcy proceedings . . . are not dictated or illuminated by principles of equity and do not fall within the judicial power of equitable subordination . . . ." *Burden*, 917 F. 2d, at 122 (Alito, J., concurring in part and dissenting in part).

Just such a legislative type of decision, however, underlies the Bankruptcy Court's reordering of priorities in question here, as approved by the District Court and the Court of Appeals. Despite language in its opinion about requiring a balancing of the equities in individual cases, the Court of Appeals actually concluded that "postpetition, nonpecuniary loss tax penalty claims" are "susceptible to subordination" by their very "nature." 48 F. 3d, at 218. And although the court said that not every tax penalty would be equitably subordinated, *ibid.*, that would be the inevitable result of consistent applications of the rule employed here, which depends not on individual equities but on the supposedly general unfairness of satisfying "postpetition, nonpecuniary loss tax penalty claims" before the claims of a general creditor.

The Court of Appeals's decision thus runs directly counter to Congress's policy judgment that a postpetition tax penalty should receive the priority of an administrative expense, 11 U.S.C. §§ 503(b)(1)(C), 507(a)(1), and 726(a)(1). This is true regardless of Noland's argument that the Bankruptcy Court made a distinction between compensatory and noncompensatory tax penalties, for this was itself a categorical distinction at a legislative level of generality. Indeed, Congress recognized and employed that distinction elsewhere in the priority provisions: Congress specifically assigned 8th priority to certain compensatory tax penalties, see § 507(a)(8)(G), and 12th priority to prepetition, noncompensatory penalties, see § 726(a)(1), and (4).[3]

The Sixth Circuit, to be sure, invoked a more modest authority than legislative revision when it relied on statements by the congressional leaders of the 1978 Code revisions, see 48 F. 3d, at 215, 217–218, and it is true that Representative Edwards and Senator DeConcini stated that "under existing law, a claim is generally subordinated only if [the] holder of such claim is guilty of inequitable conduct, or the claim itself is of a status susceptible to subordination, such as a penalty or a claim for damages arising from the purchase or sale of a security of the debtor." 124 Cong. Rec. 32398 (1978) (Rep. Edwards); see also *id.*, at 33998 (Sen. DeConcini). But their remarks were not statements of existing law and the Sixth Circuit's reliance on the unexplained reference to subordinated penalties ran counter to this Court's previous endorsement of priority treatment for postpetition tax penalties. See *Nicholas* v. *United States*, 384 U. S. 678, 692–695 (1966). More fundamentally, statements in legislative history cannot be read to convert statutory leeway for judicial development of a rule on particularized exceptions into delegated authority to revise statutory categorization, untethered to any obligation to preserve the coherence of substantive congressional judgments.

Given our conclusion that the Sixth Circuit's rationale was inappropriately categorical in nature, we need not decide today whether a bankruptcy court must always find creditor misconduct before a claim may be equitably subordinated. We do hold that (in the absence of a need to reconcile conflicting congressional choices) the circumstances that prompt a court to order equitable subordination must not occur at the level of policy choice at which Congress itself operated in drafting the Bankruptcy Code. Cf. *In re Ahlswede*, 516 F. 2d 784, 787 (CA9) ("[T]he [equity] chancellor never did, and does not now, exercise unrestricted power to contradict statutory or common law when he feels

[3] Noland argues that "although the penalties at issue arose postpetition," this claim should be viewed as a prepetition penalty because a "reorganized debtor is in many respects similar to a prepetition debtor . . . [and] the conversion of [this] case to chapter 7 was tantamount to the filing of a new petition." Brief for Respondent 16, n. 7. But we agree with the Sixth Circuit, see *In re First Truck Lines, Inc.*, 48 F. 3d 210, 214 (1995), that the penalties at issue here are postpetition administrative expenses pursuant to 11 U. S. C. §§ 348(d), 503(b)(1). Although § 348(d) provides that a "claim against the estate or the debtor that arises after the order for relief but before conversion in a case that is converted under section 1112, 1208, or 1307 of this title, other than a claim specified in section 503(b) of this title, shall be treated for all purposes as if such claim had arisen immediately before the date of the filing of the petition," the claim for priority here is "specified in section 503(b)" and Congress has already determined that it is not to be treated like prepetition penalties. Noland may or may not have a valid policy argument, but it is up to Congress, not this Court, to revise the determination if it so chooses.

a fairer result may be obtained by application of a different rule''), cert. denied *sub nom. Stebbins* v. *Crocker Citizens Nat. Bank*, 423 U.S. 913 (1975); *In re Columbia Ribbon Co.*, 117 F. 2d 999, 1002 (CA3 1941) (court cannot ''set up a subclassification of claims . . . and fix an order of priority for the sub-classes according to its theory of equity'').

In this instance, Congress could have, but did not, deny noncompensatory, postpetition tax penalties the first priority given to other administrative expenses, and bankruptcy courts may not take it upon themselves to make that categorical determination under the guise of equitable subordination. The judgment of the Court of Appeals is reversed, and the case is remanded for further proceedings consistent with this opinion.

It is so ordered.

Section 6512.—Limitations in Case of Petition to Tax Court

Ct.D. 2058

SUPREME COURT OF THE UNITED STATES

No. 94–1785

COMMISSIONER OF INTERNAL REVENUE, PETITIONER v. ROBERT F. LUNDY

516 U.S.—

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

January 17, 1996

Syllabus

Respondent Lundy and his wife withheld from their 1987 wages substantially more in federal income taxes than they actually owed for that year, but they did not file their 1987 tax return when it was due, nor did they file a return or claim a refund of the overpaid taxes in the succeeding 2½ years. On September 26, 1990, the Commissioner of Internal Revenue mailed Lundy a notice of deficiency for 1987. Some three months later, the Lundys filed their joint 1987 tax return, which claimed a refund of their overpaid taxes, and Lundy filed a timely petition in the Tax Court seeking a redetermination of the claimed deficiency and a refund. The Tax Court held that where, as here, a taxpayer has not filed a tax return by the time a notice of deficiency is mailed, and the notice is mailed more than two years after the date on which the taxes are paid, a 2-year ''look-back'' period applies under 26 U. S. C. § 6512(b)(3)(B), and the court lacks jurisdiction to award a refund. The Fourth Circuit reversed, finding that the applicable look-back period in these circumstances is three years and that the Tax Court had jurisdiction to award a refund.

Held: The Tax Court lacks jurisdiction to award a refund of taxes paid more than two years prior to the date on which the Commissioner mailed the taxpayer a notice of deficiency, if, on the date that the notice was mailed, the taxpayer had not yet filed a return. In these circumstances, the applicable look-back period under § 6512(b)(3)(B) is two years.

(a) Section 6512(b)(3)(B) forbids the Tax Court to award a refund unless it first determines that the taxes were paid ''within the [look-back] period which would be applicable under section 6511(b)(2) . . . if on the date of the mailing of the notice of deficiency a claim [for refund] had been filed.'' Section § 6511(b)(2)(A) in turn instructs the court to apply a 3-year look-back period if a refund claim is filed, as required by § 6511(a), ''within 3 years from the time the return was filed,'' while § 6511(b)(2)(B) specifies a 2-year look-back period if the refund claim is not filed within that 3-year period. The Tax Court properly applied the 2-year look-back period to Lundy's case because, as of September 26, 1990 (the date the notice of deficiency was mailed), Lundy had not filed a tax return, and, consequently, a claim filed on that date would not be filed within the 3-year period described in § 6511(a). Lundy's taxes were withheld from his wages, so they are deemed paid on the date his 1987 tax return was due (April 15, 1988), which is more than two years prior to the date the notice of deficiency was mailed. Lundy is therefore seeking a refund of taxes paid outside the applicable look-back period, and the Tax Court lacks jurisdiction to award a refund.

(b) Lundy suggests two alternative interpretations of § 6512(b)(3)(B), neither of which is persuasive. Lundy first adopts the Fourth Circuit's view, which is that the applicable look-back period is determined by reference to the date that the taxpayer *actually filed* a claim for refund, and argues that he is entitled to a 3-year look-back period because his late-filed 1987 tax return contained a refund claim that was filed within three years from the filing of the return itself. This interpretation is contrary to the requirements of the statute and leads to a result that Congress could not have intended, as it in some circumstances subjects a timely filer of a return to a shorter limitations period in Tax Court than a delinquent filer. Lundy's second argument, that the ''claim'' contemplated by § 6512(b)(3)(B) can only be a claim filed on a tax return, such that a uniform 3-year look-back period applies under that section, is similarly contrary to the language of the statute.

(c) This Court is bound by § 6512(b)(3)(B)'s language as it is written, and even if the Court were persuaded by Lundy's policy-based arguments for applying a 3-year look-back period, the Court is not free to rewrite the statute simply because its effects might be susceptible of improvement.

45 F. 3d 856, reversed.

O'CONNOR, J., delivered the opinion of the Court, in which REHNQUIST, C. J., and SCALIA, KENNEDY, SOUTER, GINSBURG, and BREYER, JJ., joined. STEVENS, J., filed a dissenting opinion. THOMAS, J., filed a dissenting opinion, in which STEVENS, J., joined.

JUSTICE O'CONNOR delivered the opinion of the Court.

In this case, we consider the ''look-back'' period for obtaining a refund of overpaid taxes in the United States Tax Court under 26 U.S.C. § 6512(b)(3)(B), and decide whether the Tax Court can award a refund of taxes paid more than two years prior to the date on which the Commissioner of Internal Revenue mailed the taxpayer a notice of deficiency, when, on the date the notice of deficiency was mailed, the taxpayer had not yet filed a return. We hold that in these circumstances the 2-year look-back period set forth in § 6512(b)(3)(B) applies, and the Tax Court lacks jurisdiction to award a refund.

I

During 1987, respondent Robert F. Lundy and his wife had $10,131 in federal income taxes withheld from their wages. This amount was substantially more than the $6,594 the Lundys actually owed in taxes for that year, but the Lundys did not file their 1987 tax return when it was due, nor did they file a return or claim a refund of the overpaid taxes in the succeeding two and a half years. On September 26, 1990, the Commissioner of Internal Revenue mailed Lundy a notice of deficiency, informing him that he owed $7,672 in additional taxes and interest for 1987 and that he was liable for substantial penalties for delinquent filing and negligent underpayment of taxes, see 26 U. S. C. §§ 6651(a)(1) and 6653(1).

Lundy and his wife mailed their joint tax return for 1987 to the Internal Revenue Service (IRS) on December 22, 1990. This return indicated that the Lundys had overpaid their income taxes for 1987 by $3,537 and claimed a refund in that amount. Two days after the return was mailed, Lundy filed a timely petition in the Tax Court seeking a redetermination of the claimed deficiency and a refund of the couple's overpaid taxes. The Commissioner filed an answer generally denying the allegations in Lundy's petition. Thereafter, the parties negotiated towards a settlement of the claimed deficiency and refund claim. On March 17, 1992, the Commissioner filed an amended answer acknowledging that Lundy had filed a tax return and that Lundy claimed to have overpaid his 1987 taxes by $3,537.

The Commissioner contended in this amended pleading that the Tax Court lacked jurisdiction to award Lundy a refund. The Commissioner argued that if a taxpayer does not file a tax return before the IRS mails the taxpayer a notice of deficiency, the Tax Court can only award the taxpayer a refund of

taxes paid within two years prior to the date the notice of deficiency was mailed. See 26 U.S.C. § 6512(b)(3)(B). Under the Commissioner's interpretation of § 6512(b)(3)(B), the Tax Court lacked jurisdiction to award Lundy a refund because Lundy's withheld taxes were deemed paid on the date that his 1987 tax return was due (April 15, 1988), see § 6513(b)(1), which is more than two years before the date the notice was mailed (September 26, 1990).

The Tax Court agreed with the position taken by the Commissioner and denied Lundy's refund claim. Citing an unbroken line of Tax Court cases adopting a similar interpretation of § 6512(b)(3)(B), *e.g. Allen* v. *Commissioner*, 99 T. C. 475, 479–480 (1992); *Galuska* v. *Commissioner*, 98 T. C. 661, 665 (1992); *Berry* v. *Commissioner*, 97 T. C. 339, 344–345 (1991); *White* v. *Commissioner*, 72 T. C. 1126, 1131–1133 (1979) (renumbered statute); *Hosking* v. *Commissioner*, 62 T. C. 635, 642–643 (1974) (renumbered statute), the Tax Court held that if a taxpayer has not filed a tax return by the time the notice of deficiency is mailed, and the notice is mailed more than two years after the date on which the taxes are paid, the look-back period under § 6512(b)(3)(B) is two years and the Tax Court lacks jurisdiction to award a refund. 65 TCM 3011, 3014–3015, RIA TC memo ¶93, 278 (1993).

The Court of Appeals for the Fourth Circuit reversed, finding that the applicable look-back period in these circumstances is three years and that the Tax Court had jurisdiction to award Lundy a refund. 45 F. 3d 856, 861 (1995). Every other Court of Appeals to have addressed the question has affirmed the Tax Court's interpretation of § 6512(b)(3)(B), see *Davison* v. *Commissioner*, 9 F. 3d 1538 (CA2 1993) (unpublished disposition); *Allen* v. *Commissioner*, 23 F. 3d 406 (CA6 1994) (unpublished disposition); *Galuska* v. *Commissioner*, 5 F. 3d 195, 196 (CA7 1993); *Richards* v. *Commissioner*, 37 F. 3d 587, 589 (CA10 1994); see also *Rossman* v. *Commissioner*, 46 F. 3d 1144 (CA9 1995) (unpublished disposition) (affirming on other grounds). We granted certiorari to resolve the conflict, 515 U. S. ___ (1995), and now reverse.

II

A taxpayer seeking a refund of overpaid taxes ordinarily must file a timely claim for a refund with the Internal Revenue Service (IRS) under 26 U. S. C. § 6511.[1] That section contains two separate provisions for determining the timeliness of a refund claim. It first establishes a *filing deadline:* The taxpayer must file a claim for a refund "within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such periods expires the later, or if no return was filed by the taxpayer, within 2 years from the time the tax was paid." § 6511(b)(1) (incorporating by reference § 6511(a)). It also defines two *"look-back" periods:* If the claim is filed "within 3 years from the time the return was filed," *ibid.*, then the taxpayer is entitled to a refund of "the portion of the tax paid within the 3 years immediately preceding the filing of the claim." § 6511(b)(2)(A) (incorporating by reference § 6511(a)). If the claim is not filed within that 3-year period, then the taxpayer is entitled to a refund of only that "portion of the tax paid during the 2 years immediately preceding the filing of the claim." § 6511(b)(2)(B) (incorporating by reference § 6511(a)).

Unlike the provisions governing refund suits in United States District Court or the United States Court of Federal Claims, which make timely filing of a refund claim a jurisdictional prerequisite to bringing suit, see 26 U.S.C. § 7422(a); *Martin* v. *United States*, 833 F. 2d 655, 658–659 (CA7 1987), the restrictions governing the Tax Court's authority to award a refund of overpaid taxes incorporate only the look-back period and not the filing deadline from § 6511. See 26 U.S.C. § 6512(b)(3).[2] Consequently, a taxpayer who seeks a refund in the Tax Court, like respondent, does not need to actually file a claim for refund with the IRS; the taxpayer need only show that the tax to be refunded was paid during the applicable look-back period.

[1] In relevant part, 26 U. S. C. § 6511 provides:

"(a) Period of limitation on filing claim

Claim for credit or refund of an overpayment of any tax imposed by this title in respect of which tax the taxpayer is required to file a return shall be filed by the taxpayer within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such periods expires the later, or if no return was filed by the taxpayer, within 2 years from the time the tax was paid. Claim for credit or refund of an overpayment of any tax imposed by this title which is required to be paid by means of a stamp shall be filed by the taxpayer within 3 years from the time the tax was paid.

"(b) Limitation on allowance of credits and refunds

"(1) Filing of claim within prescribed period

No credit or refund shall be allowed or made after the expiration of the period of limitation prescribed in subsection (a) for the filing of a claim for credit or refund, unless a claim for credit or refund is filed by the taxpayer within such period.

"(2) Limit on amount of credit or refund

"(A) Limit where claim filed within 3-year period

If the claim was filed by the taxpayer during the 3-year period prescribed in subsection (a), the amount of the credit or refund shall not exceed the portion of the tax paid within the period, immediately preceding the filing of the claim, equal to 3 years plus the period of any extension of time for filing the return. If the tax was required to be paid by means of a stamp, the amount of the credit or refund shall not exceed the portion of the tax paid within the 3 years immediately preceding the filing of the claim.

"(B) Limit where claim not filed within 3-year period

If the claim was not filed within such 3-year period, the amount of the credit or refund shall not exceed the portion of the tax paid during the 2 years immediately preceding the filing of the claim.

"(C) Limit if no claim filed

If no claim was filed, the credit or refund shall not exceed the amount which would be allowable under subparagraph (A) or (B), as the case may be, if claim was filed on the date the credit or refund is allowed."

[2] In relevant part, 26 U. S. C. § 6512(b) provides:

"(1) Jurisdiction to determine

Except as provided by paragraph (3) and by section 7463, if the Tax Court finds that there is no deficiency and further finds that the taxpayer has made an overpayment of income tax for the same taxable year . . . in respect of which the Secretary determined the deficiency, or finds that there is a deficiency but that the taxpayer has made an overpayment of such tax, the Tax Court shall have jurisdiction to determine the amount of such overpayment, and such amount shall, when the decision of the Tax Court has become final, be credited or refunded to the taxpayer.

. . . . . .

"(3) Limit on amount of credit or refund

No such credit or refund shall be allowed or made of any portion of the tax unless the Tax Court determines as part of its decision that such portion was paid—

"(A) after the mailing of the notice of deficiency,

"(B) within the period which would be applicable under section 6511(b)(2), (c), or (d), if on the date of the mailing of the notice of deficiency a claim had been filed (whether or not filed) stating the grounds upon which the Tax Court finds that there is an overpayment, or

"(C) within the period which would be applicable under section 6511(b)(2), (c), or (d), in respect of any claim for refund filed within the applicable period specified in section 6511 and before the date of the mailing of the notice of deficiency"

"(i) which had not been disallowed before that date,

"(ii) which had been disallowed before that date and in respect of which a timely suit for refund could have been commenced as of that date, or

"(iii) in respect of which a suit for refund had been commenced before that date and within the period specified in section 6532."

In this case, the applicable look-back period is set forth in § 6512(b)(3)(B), which provides that the Tax Court cannot award a refund of any overpaid taxes unless it first determines that the taxes were paid:

> "within the period which would be applicable under section 6511(b)(2) . . . if on the date of the mailing of the notice of deficiency a claim had been filed (whether or not filed) stating the grounds upon which the Tax Court finds that there is an overpayment."

The analysis dictated by § 6512(b)(3)(B) is not elegant, but it is straightforward. Though some courts have adverted to the filing of a "deemed claim," see *Galuska*, 5 F. 3d, at 196; *Richards*, 37 F. 3d, at 589, all that matters for the proper application of § 6512(b)(3)(B) is that the "claim" contemplated in that section be treated as the only mechanism for determining whether a taxpayer can recover a refund. Section 6512(b)(3)(B) defines the look-back period that applies in Tax Court by incorporating the look-back provisions from § 6511(b)(2), and directs the Tax Court to determine the applicable period by inquiring into the timeliness of a hypothetical claim for refund filed "on the date of the mailing of the notice of deficiency."

To this end, § 6512(b)(3)(B) directs the Tax Court's attention to § 6511(b)(2), which in turn instructs the court to apply either a 3-year or a 2-year look-back period. See §§ 6511(b)(2)(A) and (B) (incorporating by reference § 6511(a)); see *supra*, at 5. To decide which of these look-back periods to apply, the Tax Court must consult the filing provisions of § 6511(a) and ask whether the claim described by § 6512(b)(3)(B)—a claim filed "on the date of the mailing of the notice of deficiency"—would be filed "within 3 years from the time the return was filed." See § 6511(b)(2)(A) (incorporating by reference § 6511(a)). If a claim filed on the date of the mailing of the notice of deficiency would be filed within that 3-year period, then the look-back period is also three years and the Tax Court has jurisdiction to award a refund of any taxes paid within three years prior to the date of the mailing of the notice of deficiency. §§ 6511(b)(2)(A) and 6512(b)(3)(B). If the claim would not be filed within that 3-year period, then the period for awarding a refund is only two years. §§ 6511(b)(2)(B) and 6512(b)(3)(B).

In this case, we must determine which of these two look-back periods to apply when the taxpayer fails to file a tax return when it is due, and the Commissioner mails the taxpayer a notice of deficiency before the taxpayer gets around to filing a late return. The Fourth Circuit held that a taxpayer in this situation is entitled to a 3-year look-back period if the taxpayer actually files a timely claim at some point in the litigation, see *infra*, at 10–11, and respondent offers additional reasons for applying a 3-year look-back period, see *infra*, at 13–17. We think the proper application of § 6512(b)(3)(B) instead requires that a 2-year look-back period be applied.

We reach this conclusion by following the instructions set out in § 6512(b)(3)(B). The operative question is whether a claim filed "on the date of the mailing of the notice of deficiency" would be filed "within 3 years from the time the return was filed." See *supra*, at 7; § 6512(b)(3)(B) (incorporating §§ 6511(b)(2) and 6511(a)). In the case of a taxpayer who does not file a return before the notice of deficiency is mailed, the claim described in § 6512(b)(3)(B) could not be filed "within 3 years from the time the return was filed." No return having been filed, there is no date from which to measure the 3-year filing period described in § 6511(a). Consequently, the claim contemplated in § 6512(b)(3)(B) would not be filed within the 3-year window described in § 6511(a), and the 3-year look-back period set out in § 6511(b)(2)(A) would not apply. The applicable look-back period is instead the default 2-year period described in § 6511(b)(2)(B), which is measured from the date of the mailing of the notice of deficiency, see § 6512(b)(3)(B). The taxpayer is entitled to a refund of any taxes paid within two years prior to the date of the mailing of the notice of deficiency.

Special rules might apply in some cases, see *e.g.*, § 6511(c) (extension of time by agreement); § 6511(d) (special limitations periods for designated items), but in the case where the taxpayer has filed a timely tax return and the IRS is claiming a deficiency in taxes from that return, the interplay of §§ 6512(b)(3)(B) and 6511(b)(2) generally ensures that the taxpayer can obtain a refund of any taxes against which the IRS is asserting a deficiency. In most cases, the notice of deficiency must be mailed within three years from the date the tax return is filed. See 26 U. S. C. §§ 6501(a) and 6503(a)(1); *Badaracco* v. *Commissioner*, 464 U. S. 386, 389, 392 (1984). Therefore, if the taxpayer has already filed a return (albeit perhaps a faulty one), any claim filed "on the date of the mailing of the notice of deficiency" would necessarily be filed within three years from the date the return is filed. In these circumstances, the applicable look-back period under § 6512(b)(3)(B) would be the 3-year period defined in § 6511(b)(2)(A), and the Tax Court would have jurisdiction to award a refund.

Therefore, in the case of a taxpayer who files a timely tax return, § 6512(b)(3)(B) usually operates to toll the filing period that might otherwise deprive the taxpayer of the opportunity to seek a refund. If a taxpayer contesting the accuracy of a previously filed tax return in Tax Court discovers for the first time during the course of litigation that he is entitled to a refund, the taxpayer can obtain a refund from the Tax Court without first filing a timely claim for refund with the IRS. It does not matter, as it would in district court, see § 7422 (incorporating §§ 6511), that the taxpayer has discovered the entitlement to a refund well after the period for filing a timely refund claim with the IRS has passed, because § 6512(b)(3)(B) applies "whether or not [a claim is] filed," and the look-back period is measured from the date of the mailing of the notice of deficiency. *Ibid.* Nor does it matter, as it might in a refund suit, see 26 CFR § 301.6402–2(b)(1) (1995), whether the taxpayer has previously apprised the IRS of the precise basis for the refund claim, because 26 U. S. C. § 6512(b)(3)(B) posits the filing of a hypothetical claim "stating the grounds upon which the Tax Court finds that there is an overpayment," § 6512(b)(3)(B).

Section 6512(b)(3)(B) treats delinquent filers of income tax returns less charitably. Whereas timely filers are virtually assured the opportunity to seek a refund in the event they are drawn into Tax Court litigation, a delinquent filer's entitlement to a refund in Tax Court depends on the date of the mailing of the notice of deficiency. Section 6512(b)(3)(B) tolls the limitations period, in that it directs the Tax Court to measure the look-back period from the date on which the notice of deficiency is mailed and not the date on which the taxpayer actually files a claim for re-

fund. But in the case of delinquent filers, § 6512(b)(3)(B) establishes only a 2-year look-back period, so the delinquent filer is not assured the opportunity to seek a refund in Tax Court: If the notice of deficiency is mailed more than two years after the taxes were paid, the Tax Court lacks jurisdiction to award the taxpayer a refund.

The Tax Court properly applied this 2-year look-back period to Lundy's case. As of September 26, 1990 (the date the notice was mailed), Lundy had not filed a tax return. Consequently, a claim filed on that date would not be filed within the 3-year period described in § 6511(a), and the 2-year period from § 6511(b)(2)(B) applies. Lundy's taxes were withheld from his wages, so they are deemed paid on the date his 1987 tax return was due (April 15, 1988), see 26 U. S. C. § 6513(b)(1), which is more than two years prior to the date the notice of deficiency was mailed (September 26, 1990). Lundy is therefore seeking a refund of taxes paid outside the applicable look-back period, and the Tax Court lacks jurisdiction to award such a refund.

III

In deciding Lundy's case, the Fourth Circuit adopted a different approach to interpreting § 6512(b)(3)(B) and applied a 3-year look-back period. Respondent supports the Fourth Circuit's rationale, but also offers an argument for applying a uniform 3-year look-back period under § 6512(b)(3)(B). We find neither position persuasive. p1The Fourth Circuit held that:

> "[T]he Tax Court, when applying the limitation provision of § 6511(b)(2) in light of § 6512(b)(3)(B), should substitute the date of the mailing of the notice of deficiency for the date on which the taxpayer filed the claim for refund, but only for the purpose of determining the benchmark date for measuring the limitation period and not for the purpose of determining whether the two-year or three-year limitation period applies." 45 F. 3d, at 861.

In other words, the Fourth Circuit held that the look-back period is *measured* from the date of the mailing of the notice of deficiency (*i.e.*, the taxpayer is entitled to a refund of any taxes paid within either two or three years prior to that date), but that that date is irrelevant in calculating the *length* of the look-back period itself. The look-back period, the Fourth Circuit held, must be defined in terms of the date that the taxpayer *actually filed* a claim for refund. *Ibid.* ("[T]he three-year limitation period applies because Lundy filed his claim for refund . . . within three years of filing his tax return"). Thus, under the Fourth Circuit's view, Lundy was entitled to a 3-year look-back period because Lundy's late-filed 1987 tax return contained a claim for refund, and that claim was filed within three years from the filing of the return. *Ibid.* (taxpayer entitled to same look-back period that would apply in district court).

Contrary to the Fourth Circuit's interpretation, the fact that Lundy actually filed a claim for a refund after the date on which the Commissioner mailed the notice of deficiency has no bearing in determining whether the Tax Court has jurisdiction to award Lundy a refund. See *supra*, at 6. Once a taxpayer files a petition with the Tax Court, the Tax Court has exclusive jurisdiction to determine the existence of a deficiency or to award a refund, see 26 U. S. C. § 6512(a), and the Tax Court's jurisdiction to award a refund is limited to those circumstances delineated in § 6512(b)(3). Section 6512(b)(3)(C) is the only provision that measures the look-back period based on a refund claim that is actually filed by the taxpayer, and that provision is inapplicable here because it only applies to refund claims filed "before the date of the mailing of the notice of deficiency." § 6512(b)(3)(C). Under § 6512(b)(3)(B), which is the provision that does apply, the Tax Court is instructed to consider only the timeliness of a claim filed "on the date of the mailing of the notice of deficiency," not the timeliness of any claim that the taxpayer might actually file.

The Fourth Circuit's rule also leads to a result that Congress could not have intended, in that it subjects the timely, not the delinquent, filer to a shorter limitations period in Tax Court. Under the Fourth Circuit's rule, the availability of a refund turns entirely on whether the taxpayer has in fact filed a claim for refund with the IRS, because it is the date of *actual filing* that determines the applicable look-back period under § 6511(b)(2) (and, by incorporation, § 6512(b)(3)(B)). See 45 F. 3d, at 861; see *supra*, at 11. This rule might "eliminate[] the inequities resulting" from adhering to the 2-year look-back period, 45 F. 3d, at 863, but it creates an even greater inequity in the case of a taxpayer who dutifully files a tax return when it is due, but does not initially claim a refund. We think our interpretation of the statute achieves an appropriate and reasonable result in this case: The taxpayer who files a timely income tax return could obtain a refund in the Tax Court under § 6512(b)(3)(B), without regard to whether the taxpayer has actually filed a timely claim for refund. See *supra*, at 8–9.

If it is the actual filing of a refund claim that determines the length of the look-back period, as the Fourth Circuit held, the filer of a timely income tax return might be out of luck. If the taxpayer does not file a claim for refund with his tax return, and the notice of deficiency arrives shortly before the 3-year period for filing a timely claim expires, see 26 U. S. C. §§ 6511(a) and (b)(1), the taxpayer might not discover his entitlement to a refund until well after the commencement of litigation in the Tax Court. But having filed a timely return, the taxpayer would be precluded by the passage of time from filing an actual claim for refund "within 3 years from the time the return was filed," as § 6511(b)(2)(A) requires. § 6511(b)(2)(A) (incorporating by reference § 6511(a)). The taxpayer would therefore be entitled only to a refund of taxes paid within two years prior to the mailing of the notice of deficiency. See § 6511(b)(2)(B); 45 F. 3d, at 861–862 (taxpayer entitled to same look-back period as would apply in district court, and look-back period is determined based on date of actual filing). It is unlikely that Congress intended for a taxpayer in Tax Court to be worse off for having filed a timely return, but that result would be compelled under the Fourth Circuit's approach.

Lundy offers an alternative reading of the statute that avoids this unreasonable result, but Lundy's approach is similarly defective. The main thrust of Lundy's argument is that the "claim" contemplated in § 6512(b)(3)(B) could be filed "within 3 years from the time the return was filed," such that the applicable look-back period under § 6512(b)(3)(B) would be three years, if the claim were itself filed on a tax return. Lundy in fact argues that Congress must have intended the claim described in § 6512(b)(3)(B) to be a claim filed on a return, because there is no other way to file a claim for refund with the IRS. Brief for Respondent 28, 30 (citing 26 CFR § 301.6402–3(a)(1) (1995). Lundy therefore argues that § 6512(b)(3)(B) incorporates a uni-

form 3-year look-back period for Tax Court cases: If the taxpayer files a timely return, the notice of deficiency (and the "claim" under § 6512(b)(3)(B)) will necessarily be filed within three years of the return and the look-back period is three years; if the taxpayer does not file a return, then the claim contemplated in § 6512(b)(3)(B) is deemed to be a claim filed with, and thus within three years of, a return and the look-back period is again three years. Like the Fourth Circuit's approach, Lundy's reading of the statute has the convenient effect of ensuring that taxpayers in Lundy's position can almost always obtain a refund if they file in Tax Court, but we are bound by the terms Congress chose to use when it drafted the statute, and we do not think that the term "claim" as it is used in § 6512(b)(3)(B) is susceptible of the interpretation Lundy has given it. The Internal Revenue Code does not define the term "claim for refund" as it is used in § 6512(b)(3)(B), cf. 26 U.S.C. § 6696(e)(2) ("For purposes of section 6694 and 6695 . . . [t]he term 'claim for refund' means a claim for refund of, or credit against, any tax imposed by subtitle A"), but it is apparent from the language of § 6512(b)(3)(B) and the statute as a whole that a claim for refund can be filed separately from a return. Section 6512(b)(3)(B) provides that the Tax Court has jurisdiction to award a refund to the extent the taxpayer would be entitled to a refund "if on the date of the mailing of the notice of deficiency *a claim* had been filed." (Emphasis added.) It does not state, as Lundy would have it, that a taxpayer is entitled to a refund if on that date "a claim and a return had been filed."

Perhaps the most compelling evidence that Congress did not intend the term "claim" in § 6512 to mean a "claim filed on a return" is the parallel use of the term "claim" in § 6511(a). Section 6511(a) indicates that a claim for refund is timely if it is "filed by the taxpayer within 3 years from the time the return was filed," and it plainly contemplates that a claim can be filed even "if no return was filed." 26 U.S.C. § 6511(a). If a claim could *only* be filed with a return, as Lundy contends, these provisions of the statute would be senseless, cf. 26 U. S. C. § 6696 (separately defining "claim for refund" and "return"), and we have been given no reason to believe that Congress meant the term "claim" to mean one thing in § 6511 but to mean something else altogether in the very next section of the statute. The interrelationship and close proximity of these provisions of the statute "presents a classic case for application of the 'normal rule of statutory construction that identical words used in different parts of the same act are intended to have the same meaning.' " *Sullivan* v. *Stroop*, 496 U. S. 478, 484 (1990) (quoting *Sorenson* v. *Secretary of Treasury*, 475 U. S. 851, 860 (1986) (internal quotation marks omitted).

The regulation Lundy cites in support of his interpretation, 26 CFR § 301.6402–3(a)(1) (1995), is consistent with our interpretation of the statute. That regulation states only that a claim must "[i]n general" be filed on a return, *ibid.*, inviting the obvious conclusion that there are some circumstances in which a claim and a return can be filed separately. We have previously recognized that even a claim that does not comply with federal regulations might suffice to toll the limitations periods under the Tax Code, see, *e.g.*, *United States* v. *Kales*, 314 U. S. 186, 194 (1941) ("notice fairly advising the Commissioner of the nature of the taxpayer's claim" tolls the limitations period, even if "it does not comply with formal requirements of the statute and regulations"), and we must assume that if Congress had intended to require that the "claim" described in § 6512(b)(3)(B) be a "claim filed on a return," it would have said so explicitly.

IV

Lundy offers two policy-based arguments for applying a 3-year look-back period under § 6512(b)(3)(B). He argues that the application of a 2-year period is contrary to Congress' broad intent in drafting § 6512(b)(3)(B), which was to preserve, not defeat, a taxpayer's claim to a refund in Tax Court, and he claims that our interpretation creates an incongruity between the limitations period that applies in Tax Court litigation and the period that would apply in a refund suit filed in district court or the Court of Federal Claims. Even if we were inclined to depart from the plain language of the statute, we would find neither of these arguments persuasive.

Lundy correctly argues that Congress intended § 6512(b)(3)(B) to permit taxpayers to seek a refund in Tax Court in circumstances in which they might otherwise be barred from filing an administrative claim for refund with the IRS. This is in fact the way § 6512(b)(3)(B) operates in a large number of cases. See *supra*, at 8–9. But that does not mean that Congress intended that § 6512(b)(3)(B) would always preserve taxpayers' ability to seek a refund. Indeed, it is apparent from the face of the statute that Congress also intended § 6512(b)(3)(B) to act sometimes as a bar to recovery. To this end, the section incorporates *both* the 2-year and the 3-year look-back periods from § 6511(b)(2), and we must assume (contrary to Lundy's reading, which provides a uniform 3-year period, see *supra*, at 13–14) that Congress intended for both those look-back periods to have some effect. Cf. *Badaracco*, 464 U. S., at 405 (Stevens, J., dissenting) ("Whatever the correct standard for construing a statute of limitations . . . surely the presumption ought to be that some limitations period is applicable"). (Emphasis deleted.)

Lundy also suggests that our interpretation of the statute creates a disparity between the limitations period that applies in Tax Court and the periods that apply in refund suits filed in district court or the Court of Federal Claims. In this regard, Lundy argues that the claim for refund he filed with his tax return on December 28 would have been timely for purposes of district court litigation because it was filed "within three years from the time the return was filed," § 6511(b)(1) (incorporating by reference § 6511(a)); see also Rev. Rul. 76–511, 1976–2 Cum. Bull. 428, and within the 3-year look-back period that would apply under § 6511(b)(2)(A). Petitioner disagrees that there is any disparity, arguing that Lundy's interpretation of the statute is wrong and that Lundy's claim for refund would not have been considered timely in district court. See Brief for Petitioner 12, 29–30 and n. 11 (citing *Miller* v. *United States*, 38 F. 3d 473, 475 (1994)).

We assume without deciding that Lundy is correct, and that a different limitations period would apply in district court, but nonetheless find in this disparity no excuse to change the limitations scheme that Congress has crafted. The rules governing litigation in Tax Court differ in many ways from the rules governing litigation in the district court and the Court of Federal Claims. Some of these differences might make the Tax Court a more favorable forum, while others may not. Compare 26 U. S. C. § 6213(a) (taxpayer can seek relief in Tax Court without first paying an assessment of taxes) with *Flora* v. *United States*, 362 U.S. 145, 177 (1960) (28 U.S.C. § 1346(a)(1) requires full

payment of the tax assessment before taxpayer can file a refund suit in district court); and compare 26 U.S.C. § 6512(b)(3)(B) (Tax Court must assume that the taxpayer has filed a claim "stating the grounds upon which the Tax Court" intends to award a refund) with 26 CFR § 301.6402–2(b)(1) (1995) (claim for refund in district court must state grounds for refund with specificity). To the extent our interpretation of § 6512(b)(3)(B) reveals a further distinction between the rules that apply in these fora, it is a distinction compelled by the statutory language, and it is a distinction Congress could rationally make. As our discussion of § 6512(b)(3)(B) demonstrates, see *supra*, at 8–9, all a taxpayer need do to preserve the ability to seek a refund in the Tax Court is comply with the law and file a timely return.

We are bound by the language of the statute as it is written, and even if the rule Lundy advocates might "accor[d] with good policy," we are not at liberty "to rewrite [the] statute because [we] might deem its effects susceptible of improvement." *Badaracco*, 464 U. S., at 398. Applying § 6512(b)(3)(B) as Congress drafted it, we find that the applicable look-back period in this case is two years, measured from the date of the mailing of the notice of deficiency. Accordingly, we find that the Tax Court lacked jurisdiction to award Lundy a refund of his overwithheld taxes. The judgment is reversed.

It is so ordered.

Subpart B.—Legislation and Related Committee Reports

Public Law 104–117
104th Congress, H.R. 2778
March 20, 1996

An Act to provide that members of the Armed Forces performing services for the peacekeeping efforts in Bosnia and Herzegovina, Croatia, and Macedonia shall be entitled to tax benefits in the same manner as if such services were performed in a combat zone, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. TREATMENT OF CERTAIN INDIVIDUALS PERFORMING SERVICES IN CERTAIN HAZARDOUS DUTY AREAS.

(a) GENERAL RULE.—For purposes of the following provisions of the Internal Revenue Code of 1986, a qualified hazardous duty area shall be treated in the same manner as if it were a combat zone (as determined under section 112 of such Code):

(1) Section 2(a)(3) (relating to special rule where deceased spouse was in missing status).

(2) Section 112 (relating to the exclusion of certain combat pay of members of the Armed Forces).

(3) Section 692 (relating to income taxes of members of Armed Forces on death).

(4) Section 2201 (relating to members of the Armed Forces dying in combat zone or by reason of combat-zone-incurred wounds, etc.).

(5) Section 3401(a)(1) (defining wages relating to combat pay for members of the Armed Forces).

(6) Section 4253(d) (relating to the taxation of phone service originating from a combat zone from members of the Armed Forces).

(7) Section 6013(f)(1) (relating to joint return where individual is in missing status).

(8) Section 7508 (relating to time for performing certain acts postponed by reason of service in combat zone).

(b) QUALIFIED HAZARDOUS DUTY AREA.—For purposes of this section, the term "qualified hazardous duty area" means Bosnia and Herzegovina, Croatia, or Macedonia, if as of the date of the enactment of this section any member of the Armed Forces of the United States is entitled to special pay under section 310 of title 37, United States Code (relating to special pay; duty subject to hostile fire or imminent danger) for services performed in such country. Such term includes any such country only during the period such entitlement is in effect. Solely for purposes of applying section 7508 of the Internal Revenue Code of 1986, in the case of an individual who is performing services as part of Operation Joint Endeavor outside the United States while deployed away from such individual's permanent duty station, the term "qualified hazardous duty area" includes, during the period for which such entitlement is in effect, any area in which such services are performed.

(c) EXCLUSION OF COMBAT PAY FROM WITHHOLDING LIMITED TO AMOUNT EXCLUDABLE FROM GROSS INCOME.—Paragraph (1) of section 3401(a) of the Internal Revenue Code of 1986 (defining wages) is amended by inserting before the semicolon the following: "to the extent remuneration for such service is excludable from gross income under such section".

(d) INCREASE IN COMBAT PAY EXCLUSION FOR OFFICERS TO HIGHEST AMOUNT APPLICABLE TO ENLISTED PERSONNEL.—

(1) IN GENERAL.—Subsection (b) of section 112 of such Code (relating to commissioned officers) is amended by striking "$500" and inserting "the maximum enlisted amount".

(2) MAXIMUM ENLISTED AMOUNT.—Subsection (c) of section 112 of such Code (relating to definitions) is amended by adding at the end the following new paragraph:

"(5) The term 'maximum enlisted amount' means, for any month, the sum of—

"(A) the highest rate of basic pay payable for such month to any enlisted member of the Armed Forces of the United States at the highest pay grade applicable to enlisted members, and

"(B) in the case of an officer entitled to special pay under section 310 of title 37, United States Code, for such month, the amount of such special pay payable to such officer for such month.".

(e) EFFECTIVE DATE.—

(1) IN GENERAL.—Except as provided in paragraph (2), the provisions of and amendments made by this section shall take effect on November 21, 1995.

(2) WITHHOLDING.—Subsection (a)(5) and the amendment made by subsection (c) shall apply to remuneration paid after the date of the enactment of this Act.

SEC. 2. EXTENSION OF INTERNAL REVENUE SERVICE USER FEES.

Subsection (c) of section 10511 of the Revenue Act of 1987 is amended by striking "October 1, 2000" and by inserting "October 1, 2003".

Approved March 20, 1996.

Part IV. Items of General Interest

Notice of Proposed Rulemaking and Notice of Public Hearing

Section 1059 Extraordinary Dividends

CO–9–96

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations relating to certain distributions made by corporations to certain corporate shareholders. The proposed regulations are necessary to clarify that certain distributions in redemption of stock are treated as extraordinary dividends notwithstanding provisions that otherwise might exempt the distributions from extraordinary dividend treatment. Corporations that receive a distribution in redemption of stock may be affected if the redemption is either part of a partial liquidation of the redeeming corporation or is not pro rata as to all shareholders. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written comments and outlines of topics to be discussed at the public hearing scheduled for Wednesday, October 2, 1996, must be received by September 16, 1996.

ADDRESSES: Send submissions to: CC:DOM:CORP:R (CO–9–96), room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R (CO–9–96), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC. The public hearing will be held in room 3313, Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the hearing, Mike Slaughter, Regulations Unit, Assistant Chief Counsel (Corporate), at (202) 622–7190 (not a toll-free number). Concerning the proposed regulations, Richard K. Passales at (202) 622–7530 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Income Tax Regulations (26 CFR part 1) relating to the extraordinary dividend provisions under section 1059 of the Internal Revenue Code. Section 1059 was added by the Deficit Reduction Act of 1984, Public Law 98–369. One of the purposes of section 1059 is to prevent a corporate shareholder from creating an artificial loss on stock. See General Explanation of the Revenue Provisions of the Deficit Reduction Act of 1984.

Section 1059(a) generally requires a corporation that receives an extraordinary dividend on stock it has not held for at least two years before the dividend announcement date to reduce its basis (but not below zero) immediately before any sale or disposition of the stock by the nontaxed portion of the dividend (generally, the amount of the dividends received deduction). If the nontaxed portion of the dividend exceeds basis, the excess generally is treated as additional gain recognized when the stock is sold. Section 1059(c) generally defines an extraordinary dividend as a dividend that equals or exceeds the threshold percentage of the taxpayer's adjusted basis in such stock.

Sections 1059(d)(6), (e)(1), and (e)(2) were enacted as part of the Tax Reform Act of 1986. Each of those sections affects the definition of extraordinary dividends contained in section 1059(c). Section 1059(d)(6) generally excludes an extraordinary dividend from section 1059(a) treatment if the distributee is an original shareholder of the distributing corporation and the earnings and profits from which the dividend is paid are attributable solely to the original shareholder. Section 1059(e)(2) generally excludes a dividend from extraordinary dividend treatment if it is a "qualifying dividend." A dividend generally is a qualifying dividend if the distributee and distributing corporations are affiliated at the time of the distribution and the distribution is out of affiliated year earnings and profits. Both sections 1059(d)(6) and (e)(2) contemplate that the distribution that otherwise would be an extraordinary dividend subject to section 1059(a) is derived from earnings and profits accumulated while the distributee corporation is a shareholder of the distributing corporation. Generally, a corporate shareholder's ability to create an artificial loss is reduced if all of the distributing corporation's earnings and profits are accumulated while the distributee corporation is a shareholder of the distributing corporation.

Section 1059(e)(1) expands the scope of the extraordinary dividend definition in section 1059(c) by disregarding the holding period and threshold rules for certain distributions. Generally, section 1059(e)(1) provides that a non pro rata redemption or a partial liquidation that is treated as a dividend under section 301 is an extraordinary dividend to which section 1059(a) applies without regard to the threshold percentage or the period the taxpayer held such stock. See General Explanation of the Tax Reform Act of 1986, Joint Committee on Taxation, 100th Cong., 1st Sess. (May 4, 1987).

These regulations address the question of whether section 1059(d)(6) or (e)(2) applies to a distribution otherwise treated as an extraordinary dividend under section 1059(e)(1). The IRS and Treasury Department believe that applying those provisions to section 1059(e)(1) is inconsistent with the purpose of section 1059 and may create inappropriate consequences, such as basis shifting that eliminates gain or creates an artificial loss.

Accordingly, these regulations clarify that neither section 1059(d)(6) nor section 1059(e)(2) applies to a distribution treated as an extraordinary dividend under section 1059(e)(1). In finalizing these regulations, the IRS and Treasury Department will consider comments that illustrate distributions described in section 1059(e)(1) to which the application of section 1059(d)(6) or (e)(2) is appropriate or to which section 1059(e)(1) otherwise should not apply.

These regulations also address the question of whether an exchange treated as a dividend under section 356(a)(2) is subject to section 1059(e)(1). These regulations clarify that for purposes of section 1059(e)(1), an exchange under section 356(a)(1) is treated as a redemption and, to the extent any amount is treated as a dividend under section 356(a)(2), it is treated as a dividend under section 301.

Explanation of Provisions

Proposed § 1.1059(e)–1(a) provides that neither section 1059(d)(6) nor section 1059(e)(2) will prevent any distribution treated as an extraordinary dividend under section 1059(e)(1) from being treated as an extraordinary dividend. For example, if a redemption of stock is not pro rata as to all shareholders, any amount treated as a dividend under section 301 is treated as an extraordinary dividend regardless of whether the dividend is a qualifying dividend.

Proposed § 1.1059(e)–1(b) provides that for purposes of section 1059(e)(1), an exchange under section 356(a)(1) is treated as a redemption and, to the extent any amount is treated as a dividend under section 356(a)(2), it is treated as a dividend under section 301.

Proposed Effective Date

These regulations are proposed to apply to distributions announced on or after June 17, 1996.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure 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. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying.

A public hearing has been scheduled at 10 a.m. on Wednesday, October 2, 1996, room 3313, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC. Because of access restrictions, visitors will not be admitted beyond the Internal Revenue Building lobby more that 15 minutes before the hearing starts.

The rules of 26 CFR 601.601(a)(3) apply to the hearing.

Persons that wish to present oral comments at the hearing must submit written comments by September 16, 1996, and submit an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by September 16, 1996.

A period of 10 minutes will be allotted to each person for making comments.

An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Richard K. Passales, Office of Assistant Chief Counsel (Corporate), IRS. However, other personnel from the IRS and Treasury Department participated in their development.

* * * * *

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 is amended by adding an entry in numerical order to read as follows:

Authority: 26 U.S.C. 7805 * * *
Section 1.1059(e)–1 also issued under 26 U.S.C. 1059(e)(1) and (e)(2). * * *

Par. 2. Section 1.1059(e)–1 is added to read as follows:

§ 1.1059(e)–1 Non pro rata redemptions.

(a) *In general.* Section 1059(d)(6) (exception where stock held during entire existence of corporation) and section 1059(e)(2) (qualifying dividends) do not apply to a distribution treated as an extraordinary dividend under section 1059(e)(1). For example, if a redemption of stock is not pro rata as to all shareholders, any amount treated as a dividend under section 301 is treated as an extraordinary dividend regardless of whether the dividend is a qualifying dividend.

(b) *Reorganizations.* For purposes of section 1059(e)(1), an exchange under section 356(a)(1) is treated as a redemption and, to the extent any amount is treated as a dividend under section 356(a)(2), it is treated as a dividend under section 301.

(c) *Effective date.* This section applies to distributions announced (within the meaning of section 1059(d)(5)) on or after June 17, 1996.

Margaret Milner Richardson,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on June 17, 1996, 8:45 a.m., and published in the issue of the Federal Register for June 18 1996, 61 F.R. 30845)

Notice of Proposed Rulemaking and Notice of Public Hearing

Mark-to-Market for Dealers in Securities; Equity Interests in Related Parties and the Dealer-Customer Relationship

FI–32–95

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations that make mark-to-market accounting inapplicable to most equity interests in related entities. The regulations also relate to the definition of a dealer in securities for certain federal income tax purposes. To qualify as a dealer in securities, a taxpayer must engage in transactions with customers. The proposed regulations concern the existence of dealer-customer relationships. The Revenue Reconciliation Act of 1993 amended the applicable tax law. These regulations provide guidance for taxpayers that engage in securities transactions. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written comments and outlines of oral comments to be presented at a public hearing scheduled for October 15, 1996, at 10 a.m., must be received by September 18, 1996.

ADDRESSES: Send submissions to: CC:DOM:CORP:R (FI–32–95), room 5228, Internal Revenue Service, POB

7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R (FI–32–95), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC 20224. The public hearing will be held in the Commissioner's Conference Room, room 3313, Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC 20224.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Jo Lynn L. Ricks, (202) 622–3920, or Robert B. Williams, (202) 622–3960; concerning submissions and the hearing, Michael Slaughter, (202) 622–7190 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

The collection of information contained in this notice of proposed rulemaking 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).

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, T:FP, Washington, DC 20224. Comments on the collection of information should be received by August 19, 1996.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

The collection of information is described in the Explanation of Provisions section of the Preamble (rather than being included in the text of the proposed regulations). The Preamble requests comments on whether the final regulations should permit taxpayers to elect to disregard certain inter-company transactions in determining status as a dealer in securities. The preamble also indicates that, if the election is allowed to be made, it is expected that taxpayers would make it by attaching a statement to a tax return. If the final regulations allow taxpayers to make this election in this manner, the information will be required by the IRS to determine whether the election has been made, and will be used for that purpose. The likely respondents will be businesses that file consolidated tax returns. If taxpayers are allowed to make the election, responses to this collection of information will be required to obtain the benefit of having status as a dealer in securities determined without regard to certain intercompany transactions.

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 tax return information are confidential, as required by 26 U.S.C. 6103.

Estimated total annual reporting burden: 6,000 hours.

The estimated annual burden per respondent varies from .25 hour to 1 hour, depending on individual circumstances, with an estimated average of .5 hours.

Estimated number of respondents: 12,000.

Estimated annual frequency of responses: once in the existence of each respondent.

Background

This document contains proposed regulations under section 475 of the Internal Revenue Code, which requires mark-to-market accounting for certain dealers in securities. Section 475 was added by section 13223 of the Revenue Reconciliation Act of 1993, Pubic Law 103–66, 107 Stat. 481, and is effective for all taxable years ending on or after December 31, 1993.

Temporary and proposed regulations published on December 29, 1993, [58 FR 68798] provide that stock in a 50-percent-controlled subsidiary (and interests in 50-percent-controlled partnerships and trusts) are deemed properly identified as held for investment and thus are excluded from mark-to-market accounting. The IRS is reproposing this rule with two changes. First, the IRS has concluded that the rationale for the rule applies equally to equity interests in most related persons and not just to persons controlled by the taxpayer. Second, after considering various comments received, the IRS determined that this rule prohibiting marking a security to market should not apply if two requirements are met: (1) the security is actively traded on a national securities exchange or through an interdealer quotation system; and (2) the taxpayer who marks owns less than 5 percent of all shares or interests of the same class. Comments are requested as to whether it is appropriate to allow any equity interests in related parties to be marked to market, and, if so, whether the proposed limitations are the most appropriate ones. The provisions in this document concerning these issues are referred to below in this preamble as the reproposed regulations.

When commenting on the temporary and proposed regulations, taxpayers asked the IRS to provide guidance on whether certain transactions are entered into with customers for purposes of section 475. Whether transactions are entered into with customers can affect both whether a taxpayer is a dealer in securities subject to mark-to-market accounting (see section 475(c)(1)) and whether a dealer may exempt a security from mark-to-market treatment (see section 475(b)(1)(A) and (B) and § 1.475(b)–1T(a)).

In response to these comments, on January 4, 1995, the IRS published proposed regulations [(FI–42–94) (60 FR 397)] stating that whether a taxpayer is transacting business with customers is determined based on all of the facts and circumstances (see proposed § 1.475(c)–1(c), reproposed as § 1.475(c)–1(a)). These proposed regulations also provide that the term dealer in securities includes a taxpayer that, in the ordinary course of its trade or business, regularly holds itself out as being willing and able to enter into either side of a transaction enumerated in section 475(c)(1)(B) (see proposed § 1.475(c)–1(c)(2), reproposed as § 1.475(c)–1(a)(2)).

On March 4, 1996, the IRS published Notice 96–12 (1996–10 I.R.B. 29), stating that the IRS intended to publish additional proposed regulations concerning when transactions with related parties may be transactions with customers for purposes of section 475. Notice 96–12 also described the substance of rules that the proposed regulations were expected to contain. The rules were expected to be proposed to be effective for taxable years beginning on or after February 20, 1996. The proposed regulations in this document generally reflect the substance that was described in Notice 96–12.

Explanation of Provisions

Prohibition against marking equity interests in related persons

The reproposed regulations identify certain assets that are inherently investments and, thus, may not be marked to market under section 475. The new rules retain the provision in the temporary regulations that prevents marking certain insurance products to market, but they differ from the temporary regulations in the provisions that prevent the marking of certain equity interests. Under the temporary regulations, the prohibition against marking applies only if the dealer in securities controls the issuer of an equity interest (whether it is stock in a corporation or an interest in a widely held or publicly traded partnership or trust). The reproposed regulations expand the scope of this treatment so that mark-to-market accounting cannot be used for equity interests in many related issuers. (For these purposes, the reproposed regulations incorporate by reference the relevant relations described in sections 267(b) and 707(b)(1).) The reproposed regulations also narrow the scope of this prohibition against marking so that mark-to-market accounting can be used for certain actively-traded securities, regardless of the dealer's relation to the issuer of the security, if the dealer owns less than five percent of the securities. The IRS is particularly interested in receiving comments on the scope of the reproposed rules' exception to the general prohibition on marking to market equity interests in a related person.

These reproposed regulations also contain rules to cover situations where a security begins, or ceases, to be subject to this deemed-identification rule. First, if a security is being marked to market and then, as a result of a change in facts, the regulations prohibit the security from continuing to be marked to market, the regulations require that the security be marked as of the close of business on the last day before the day when the prohibition on marking first applies.

Second, the reproposed regulations also cover situations in which the regulations have prohibited a security from being marked to market and then the prohibition on marking ceases to apply. In these cases, the deadline for the taxpayer to identify the security under section 475(b)(2) as exempt from mark-to-market treatment is generally extended until the date the prohibition on marking ceases to apply. (If the taxpayer had identified the security by the original deadline, the extension, of course, is irrelevant.) If the identification is not made on or before the deadline (as so extended), new changes in value are taken into account under the mark-to-market method, but recognition of appreciation and depreciation that occurred while the security was not being marked is suspended. This is the approach adopted by section 475(b)(3) for securities that lose their exemption from mark-to-market treatment. The proposed rule is to apply both when the prohibition on marking ceases because of a change in facts and when the prohibition on marking ceases because the rule covering certain actively-traded securities becomes effective.

In sum, under the reproposed regulations, the following assets held by a dealer in securities are deemed to be properly identified as held for investment: (1) stock in a corporation (or a partnership or beneficial ownership interest in a widely held or publicly traded partnership or trust) to which the taxpayer is related (other than certain actively-traded stock or interests); and (2) an annuity, endowment, or life insurance contract. The provision concerning the second category of assets continues to be proposed to apply to all taxable years ending on or after December 31, 1993. The rules concerning the first category of assets, however, are proposed to prohibit only those marks to market that would have occurred on or after June 19, 1996. If the prohibition against marking begins to apply to a security solely because of this effective date rule, then (unlike the situation when the onset of the prohibition is caused by a change in facts) the security is not marked to market immediately before the prohibition begins.

In general, the provision allowing certain actively-traded securities to be marked to market even when the issuer of the security is related is proposed to be effective for marks to market on or after June 19, 1996. Thus, this effective date is the same as the effective date in the reproposed regulations for the general prohibition on marking to market securities issued by a related person. Until the reproposed regulations are finalized, however, all equity interests issued by controlled entities continue to be subject to the temporary regulations' prohibition against being marked to market, even if the dealer owns less than 5 percent of interests of that class and even if the interests are actively traded.

Some commenters suggested there should be no per se rule treating certain securities as held for investment, but instead there should be a rebuttable presumption to this effect for these items. Other commenters proposed to add, or delete, a variety of items to or from those deemed to be per se held for investment. The reproposed regulations do not adopt these suggestions.

Consolidated Returns

Under both the temporary and the reproposed regulations, there are situations in which the mark-to-market method may apply to a consolidated group member's stock held by another member of the group. This may result in the recognition of duplicate gain or loss. For instance, if a common parent marks to market stock in a subsidiary to reflect increases in the value of the subsidiary stock owned by the parent resulting from appreciation in the value of the subsidiary's assets, the parent will recognize gain on that stock under the mark-to-market method. The subsidiary's subsequent sale of the assets will replicate that gain at the subsidiary level. The gains will generate duplicate stock basis increases under section 475 and § 1.1502–32(b), creating the potential for an offsetting loss when the stock is subsequently marked down to fair market value under section 475. Section 1.1502–20, however, may disallow any such offsetting loss. Comments are invited regarding how to address the anomalies these rules may produce.

The dealer-customer relationship

These proposed regulations clarify that a taxpayer's transactions with members of its consolidated group or other related persons may be transactions with customers for purposes of section 475. Thus, a taxpayer may be a dealer in securities for purposes of section 475 even if its only customer transactions are transactions with members of its consolidated group. In enacting section 475, Congress adopted a taxpayer-by-taxpayer approach to determining dealer status, rather than the single-entity approach embodied in § 1.1502–13.

An example in the proposed regulations clarifies that, for purposes of section 475, transactions do not fail to be transactions with customers solely because the parties enter into them with

other than arms-length pricing terms. Under section 482 and the regulations thereunder, however, the district director may make allocations between or among the members of the group if he or she determines that a member has not reported its true taxable income.

These proposed regulations generally reflect the substance of the rules set forth in Notice 96–12 (1996–10 I.R.B. 29). In response to taxpayer comments, however, certain language in Notice 96–12 has been clarified. Because of these changes, although the rules described in Notice 96–12 were expected to be proposed to be effective for taxable years beginning on or after February 20, 1996, these proposed regulations are to be effective for taxable years beginning on or after June 20, 1996. If there are any situations in which the proposed rules lead to a different result from that which would be reached under the rules described in the notice, a taxpayer may reasonably and consistently apply the rules described in the notice for any taxable year beginning on or after February 20, 1996, and before June 20, 1996.

Under these regulations, a taxpayer may be a dealer in securities based solely on transactions with other members of its consolidated group. The IRS requests comments on whether certain consolidated groups should be allowed to disregard inter-member transactions in determining a member's status as a dealer in securities. For instance, a group might be allowed to disregard inter-member transactions if the group, considered as a single corporation, would not be a dealer in securities for purposes of section 475. It is likely that the election, if permitted by the final regulations, would be made by attaching an appropriate statement to the taxpayer's return. (See the Paperwork Reduction Act section of this preamble, which requests comments on the burden that might be imposed by this requirement.) The IRS hereby requests comments on the desirability and potential terms and conditions of any such election. Comments could also address whether such an election should apply in determining whether a taxpayer had made more than negligible sales for purposes of reproposed § 1.475(c)–1(c). Further, the IRS requests comments on whether the election should be available only to groups that have not made a separate-entity election under § 1.1221–2(d)(2).

Miscellaneous

Some of the 1993 and 1995 proposed regulations are reordered.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure 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. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying.

A public hearing has been scheduled for October 15, 1996, at 10 a.m. in the Commissioner's Conference Room, room 3313, Internal Revenue Building, 1111 Constitution Avenue NW., Washington, DC 20224. Because of access restrictions, visitors will not be admitted beyond the Internal Revenue Building lobby more than 15 minutes before the hearing starts.

The rules of 26 CFR 601.601(a)(3) apply to the hearing.

Persons that wish to present oral comments at the hearing must submit written comments and submit an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by September 18, 1996.

A period of 10 minutes will be allotted to each person for making comments.

An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal authors of these regulations are Jo Lynn L. Ricks and Robert B. Williams, Office of Assistant Chief Counsel (Financial Institutions & Products). However, other personnel from the IRS and Treasury Department participated in their development.

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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, as proposed on January 4, 1995, at 60 FR 401, is further amended by revising the entries for "Section 1.475(b)–1", "Section 1.475(b)–2", and "Section 1.475(b)–4" to read as follows:

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

Section 1.475(b)–1 also issued under 26 U.S.C. 475(a) and 26 U.S.C. 475(e).

Section 1.475(b)–2 also issued under 26 U.S.C. 475(b)(2) and 26 U.S.C. 475(e). * * *

Section 1.475(b)–4 also issued under 26 U.S.C. 475(b)(2), 26 U.S.C. 475(e), and 26 U.S.C. 6001. * * *

Par. 2. Section 1.475–0, as proposed on January 4, 1995 (60 FR 401), is amended by:

1. Revising the heading and entries for § § 1.475(b)–1, 1.475(b)–2, and 1.475(b)–4.

2. Revising the entries under §§ 1.475(c)–1 and 1.475(c)–2.

3. Removing the entries under § 1.475(e)–1.

The revisions read as follows:

§ 1.475–0 Table of contents.

* * * * *

§ 1.475(b)–1 Scope of exemptions from mark-to-market requirement.

(a) Securities held for investment or not held for sale.
(b) Securities deemed identified as held for investment.
  (1) In general.
  (2) Relationships
    (i) General rule
    (ii) Attribution
    (iii) Trusts treated as partnerships
  (3) Securities traded on certain established financial markets.
  (4) Changes in status.
    (i) Onset of prohibition against marking.
    (ii) Termination of prohibition against marking.
    (iii) Examples
(c) Securities deemed not held for investment.

(1) General rule for dealers in notional principal contracts and derivatives.
(2) Exception for securities not acquired in dealer capacity.
(d) Special rules.
(1) Stock, partnership, and beneficial ownership interests in certain controlled corporations, partnerships, and trusts.
(i) In general.
(ii) Control defined.
(iii) Applicability.
(2) [Reserved]

§ 1.475(b)–2 Exemptions—Identification requirements.

(a) Identification of the basis for exemption.
(b) Time for identifying a security with a substituted basis.
(c) Securities involved in integrated transactions under § 1.1275–6.
(1) Definitions.
(2) Synthetic debt held by a taxpayer as a result of legging in.
(3) Securities held after legging out.

* * * * *

§ 1.475(b)–4 Exemptions—Transitional issues.

(a) Transitional identification.
(1) Certain securities previously identified under section 1236.
(2) Consistency requirement for other securities.
(b) Corrections on or before January 31, 1994.
(1) Purpose.
(2) To conform to § 1.475(b)–1(a).
(i) Added identifications.
(ii) Limitations.
(3) To conform to § 1.475(b)–1(c).
(c) Effect of corrections.

§ 1.475(c)–1 Definitions—Dealer in securities.

(a) Dealer-customer relationship.
(1) [Reserved].
(2) Transactions described in section 475(c)(1)(B).
(i) In general.
(ii) Examples.
(3) Related parties.
(i) In general.
(ii) Example.
(b) Sellers of nonfinancial goods and services.
(c) Taxpayers that purchase securities but do not sell more than a negligible portion of the securities.
(1) Exemption from dealer status.
(2) Negligible portion.
(3) Special rules.
(d) Issuance of life insurance products.

§ 1.475(c)–2 Definitions—Security.

(a) In general.
(b) Synthetic debt held by a taxpayer as a result of an integrated transaction under § 1.1275–6.
(c) Negative value REMIC residuals.
(d) Special rules.

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§ 1.475(e)–1 Effective dates.

Par. 3. Section 1.475(b)–1 as proposed on December 29, 1993 (58 FR 68798), is amended by revising paragraph (b) and adding paragraph (d) to read as follows:

§ 1.475(b)–1 Scope of exemptions from mark-to-market requirement.

* * * * *

(b) *Securities deemed identified as held for investment*—(1) *In general.* The following items held by a dealer in securities are per se held for investment within the meaning of section 475(b)(1)(A) and are deemed to be properly identified as such for purposes of section 475(b)(2)—

(i) Except as provided in paragraph (b)(3) of this section, stock in a corporation, or a partnership or beneficial ownership interest in a widely held or publicly traded partnership or trust, to which the taxpayer has a relationship specified in paragraph (b)(2) of this section; or

(ii) A contract that is treated for federal income tax purposes as an annuity, endowment, or life insurance contract (see sections 817 and 7702).

(2) *Relationships*—(i) *General rule.* The relationships specified in this paragraph (b)(2) are—

(A) those described in section 267(b)(2), (3), (10), (11), or (12); or

(B) those described in section 707(b)(1)(A) or (B).

(ii) *Attribution.* The relationships described in paragraph (b)(2)(i) of this section are determined taking into account sections 267(c) and 707(b)(3), as appropriate.

(iii) *Trusts treated as partnerships.* For purposes of this paragraph (b)(2), the phrase partnership or trust is substituted for the word partnership in sections 707(b)(1) and 707(b)(3), and a reference to beneficial ownership interest is added to each reference to capital interest or profits interest in those sections.

(3) *Securities traded on certain established financial markets.* Paragraph (b)(1)(i) of this section does not apply to a security if—

(i) The security is actively traded within the meaning of § 1.1092(d)–1(a) taking into account only established financial markets identified in § 1.1092(d)–1(b)(1)(i) or (ii) (describing national securities exchanges and interdealer quotation systems), and

(ii) The taxpayer owns less than 5 percent of all of the shares or interests in the same class.

(4) *Changes in status*—(i) *Onset of prohibition against marking*—(A) Once a security begins to be described in paragraph (b)(1) of this section and for so long as it continues to be so described, section 475(a) does not apply to the security in the hands of the taxpayer.

(B) If a security has not been timely identified under section 475(b)(2) and, after the last day on which such an identification would have been timely, the security begins to be described in paragraph (b)(1) of this section, then the dealer must recognize gain or loss on the security as if it were sold for its fair market value as of the close of business of the last day before the security begins to be described in paragraph (b)(1) of this section, and gain or loss is taken into account at that time.

(ii) *Termination of prohibition against marking.* If a taxpayer did not timely identify a security under section 475(b)(2) and paragraph (b)(1) of this section applies to the security on the last day on which such an identification would have been timely but it thereafter ceases to apply—

(A) An identification of the security under section 475(b)(2) is timely if made on or before the close of the day paragraph (b)(1) of this section ceases to apply; and

(B) Unless the taxpayer timely identifies the security under section 475(b)(2) (taking into account the additional time for identification that is provided by paragraph (b)(4)(ii)(A) of this section), section 475(a) applies to changes in value of the security after the cessation in the same manner as under section 475(b)(3).

(iii) *Examples.* These examples illustrate this paragraph (b)(4):

Example 1. Onset of prohibition against marking—(A) *Facts.* Corporation H owns 75 percent of the stock of corporation *D*, a dealer in securities within the meaning of section 475(c)(1). On December 1, 1995, *D* acquired less than half of the stock in corporation *X*. *D* did not identify the stock for purposes of section 475(b)(2). On July

17, 1996, *H* acquired from other persons 70 percent of the stock of *X*. As a result, *D* and *X* became related within the meaning of paragraph (b)(2)(i) of this section. The stock of *X* is not described in paragraph (b)(3) of this section (concerning securities traded on certain established financial markets).

(B) *Holding.* Under paragraph (b)(4)(i) of this section, *D* recognizes gain or loss on its *X* stock as if the stock were sold for its fair market value at the close of business on July 16, 1996, and the gain or loss is taken into account at that time. As with any application of section 475(a), proper adjustment is made in the amount of any gain or loss subsequently realized. After July 16, 1996, section 475(a) does not apply to *D*'s *X* stock while *D* and *X* continue to be related to each other.

Example 2. Termination of prohibition against marking; retained securities identified as held for investment—(A) *Facts.* On July 1, 1996, corporation *H* owned 60 percent of the stock of corporation *Y* and all of the stock of corporation *D*, a dealer in securities within the meaning of section 475(c)(1). Thus, *D* and *Y* are related within the meaning of paragraph (b)(2)(i) of this section. Also on July 1, 1996, *D* acquired, as an investment, 10 percent of the stock of *Y*. The stock of *Y* is not described in paragraph (b)(3) of this section (concerning securities traded on certain established financial markets). When *D* acquired its shares of *Y* stock, it did not identify them for purposes of section 475(b)(2). On December 27, 1996, *D* identified its shares of *Y* stock as held for investment under section 475(b)(2). On December 30, 1996, *H* sold all of its shares of stock in *Y* to an unrelated party. As a result, *D* and *Y* cease to be related within the meaning of paragraph (b)(2)(i) of this section.

(B) *Holding.* Under paragraph (b)(4)(ii)(A) of this section, identification of the *Y* shares is timely if done on or before the close of December 30, 1996. Because *D* timely identified its *Y* shares under section 475(b)(2), it continues to refrain from marking to market its *Y* stock after December 30, 1996.

Example 3. Termination of prohibition against marking; retained securities not identified as held for investment—(A) *Facts.* The facts are the same as in *Example 2* above, except that *D* did not identify its stock in *Y* for purposes of section 475(b)(2) on or before December 30, 1996. Thus, *D* did not timely identify these securities under section 475(b)(2) (taking into account the additional time for identification provided in paragraph (b)(4)(ii)(A) of this section).

(B) *Holding.* Under paragraph (b)(4)(ii)(B) of this section, section 475(a) applies to changes in value of *D*'s *Y* stock after December 30, 1996, in the same manner as under section 475(b)(3). Thus, any appreciation or depreciation that occurred while the securities were prohibited from being marked to market is suspended. Further, section 475(a) applies only to those changes occurring after December 30, 1996.

* * * * *

(d) *Special rules*—(1) *Stock, partnership, and beneficial ownership interests in certain controlled corporations, partnerships, and trusts*—(i) *In general.* The following items held by a dealer in securities are per se held for investment within the meaning of section 475(b)(1)(A) and are deemed to be properly identified as such for purposes of section 475(b)(2)—

(A) Stock in a corporation that the taxpayer controls (within the meaning of paragraph (d)(1)(ii) of this section); or

(B) A partnership or beneficial ownership interest in a widely held or publicly traded partnership or trust that the taxpayer controls (within the meaning of paragraph (d)(1)(ii) of this section).

(ii) *Control defined.* Control means the ownership, directly or indirectly through persons described in section 267(b) (taking into account section 267(c)), of—

(A) 50 percent or more of the total combined voting power of all classes of stock entitled to vote; or

(B) 50 percent or more of the capital interest, the profits interest, or the beneficial ownership interest in the widely held or publicly traded partnership or trust.

(iii) *Applicability.* The rules of this paragraph (d)(1) apply only before the date 30 days after final regulations on this subject are published in the **Federal Register**.

(2) [Reserved].

Par. 4. Section 1.475(b)–2, as proposed on December 29, 1993 (58 FR 68798), is redesignated as § 1.475(b)–4.

Par. 5. Section 1.475(b)–4, as proposed on January 4, 1995 (60 FR 404), is redesignated as § 1.475(b)–2.

Par. 6. Section 1.475(c)–1, as proposed on December 29, 1993 (58 FR 68798), and amended on January 4, 1995 (60 FR 405), is amended as follows:

1. Paragraph (c) is removed.

2. Paragraphs (a) and (b) are redesignated as paragraphs (b)and (c), respectively.

3. New paragraph (a) is added to read as follows:

§ 1.475(c)–1 Definitions—Dealer in securities.

(a) *Dealer-customer relationship.* Whether a taxpayer is transacting business with customers is determined on the basis of all of the facts and circumstances.

(1) [Reserved].

(2) *Transactions described in section 475(c)(1)(B)*—(i) *In general.* For purposes of section 475(c)(1)(B), the term dealer in securities includes, but is not limited to, a taxpayer that, in the ordinary course of the taxpayer's trade or business, regularly holds itself out as being willing and able to enter into either side of a transaction enumerated in section 475(c)(1)(B).

(ii) *Examples.* The following examples illustrate the rules of this paragraph (a)(2). In the following examples, *B* is a bank:

Example 1. B regularly offers to enter into interest rate swaps with other persons in the ordinary course of its trade or business. *B* is willing to enter into interest rate swaps under which it either pays a fixed interest rate and receives a floating rate or pays a floating rate and receives a fixed rate. *B* is a dealer in securities under section 475(c)(1)(B), and the counterparties are its customers.

Example 2. B, in the ordinary course of its trade or business, regularly holds itself out as being willing and able to enter into either side of positions in a foreign currency with other banks in the interbank market. *B*'s activities in the foreign currency make it a dealer in securities under section 475(c)(1)(B), and the other banks in the interbank market are its customers.

Example 3. B engages in frequent transactions in a foreign currency in the interbank market. Unlike the facts in *Example 2*, however, *B* does not regularly hold itself out as being willing and able to enter into either side of positions in the foreign currency, and all of *B*'s transactions are driven by its internal need to adjust its position in the currency. No other circumstances are present to suggest that *B* is a dealer in securities for purposes of section 475(c)(1)(B). *B*'s activity in the foreign currency does not qualify it as a dealer in securities for purposes of section 475(c)(1)(B), and its transactions in the interbank market are not transactions with customers.

(3) *Related parties*—(i) *In general.* A taxpayer's transactions with members of its consolidated group or with other related persons may be transactions with customers for purposes of section 475. For example, transactions enumerated in section 475(c)(1)(B) between members of a consolidated group are transactions with customers if, in the ordinary course of its business, the taxpayer holds itself out as being willing and able to engage in these transactions on a regular basis. A taxpayer may be a dealer in securities within the meaning of section 475(c)(1) even if its only customer transactions are transactions with other members of its consolidated group.

(ii) *Example.* The following example illustrates this paragraph (a)(3):

Example. Risk management transactions—(1) *Facts. HC*, a hedging center, provides interest rate hedges to all of the members of its consolidated group. Because of the efficiencies created by having a centralized risk manager, group policy prohibits members other than *HC* from entering into derivative interest rate positions with outside parties. *HC* regularly holds itself out as being willing and able to, and in fact does, enter into either side of interest rate swaps with its fellow members. *HC* periodically computes its aggregate position and hedges the net risk with an unrelated party. *HC* does not otherwise enter into interest rate positions with persons that are not members of the consolidated group. Because *HC* attempts to operate at cost and the terms of its swaps do not

factor in any risk of default by the affiliate, *HC*'s affiliates receive somewhat more favorable terms then they would receive from an unrelated swaps dealer.

(2) *Holding*. Because *HC* regularly holds itself out as being willing and able to enter into transactions enumerated in section 475(c)(1)(B), *HC* is a dealer in securities for purposes of section 475(c)(1)(B) and the other members are its customers.

* * * * *

Par. 7. Section 1.475(c)–2, as proposed on December 29, 1993 (58 FR 68798), and amended on January 4, 1995 (60 FR 405), is amended as follows:

1. Paragraphs (b), (c), and (d) are redesignated as paragraphs (c), (d), and (b), respectively.

2. Paragraph (a) and newly designated paragraph (c) are revised by removing the phrase "paragraph (b)" each place it appears and replacing it with "paragraph (c)" each place it appeared.

3. Newly designated paragraph (d) is revised by removing the phrase "paragraphs (a)(3) and (b)" and replacing it with "paragraphs (a)(3) and (c)". Newly designated paragraph (d) is further revised by removing the phrase "this paragraph (c)(1))." and replacing it with the phrase "this paragraph (d)(1)).".

4. Newly designated paragraph (b) is revised by removing the words "See § 1.475(b)–4(c)" and replacing them with the words "See § 1.475(b)–2(c)".

Par. 8. Section 1.475(e)–1, as proposed on December 29, 1993 (58 FR 68798), and amended on January 4, 1995 (60 FR 405), is revised to read as follows:

§ 1.475(e)–1 Effective dates.

(a) Section 1.475(a)–1 (concerning mark-to-market for debt instruments) applies to taxable years beginning on or after January 1, 1995.

(b) Section 1.475(a)–2 (concerning marking a security to market upon disposition) applies to dispositions or terminations of ownership occurring on or after January 4, 1995.

(c) Section 1.475(a)–3 (concerning acquisition by a dealer of a security with a substituted basis) applies to securities acquired, originated, or entered into on or after January 4, 1995.

(d) Section 1.475(b)–1 (concerning the scope of exemptions from the mark-to-market requirement) applies as follows:

(1) Section 1.475(b)–1(a) (concerning securities held for investment or not held for sale) applies to taxable years ending on or after December 31, 1993.

(2) Except as provided elsewhere in this paragraph (d)(2), § 1.475(b)–1(b)(1) (concerning securities deemed identified as held for investment) applies to taxable years ending on or after December 31, 1993.

(i) Section 1.475(b)–1(b)(1)(i) (concerning equity interests issued by a related person) applies on or after June 19, 1996. If, on June 18, 1996, a security is subject to mark-to-market accounting and, on June 19, 1996, § 1.475(b)–1(b)(1) begins to apply to the security solely because of the effective dates in this paragraph (d)(2) (rather than because of a change in facts), then the rules of § 1.475(b)–1(b)(4)(i)(A) (concerning the prohibition against marking) apply, but § 1.475(b)–1(b)-(4)(i)(B) (imposing a mark to market on the day before the onset of the prohibition) does not apply.

(ii) Section 1.475(b)–1(b)(2) (concerning relevant relationships for purposes of determining whether equity interests in related persons are prohibited from being marked to market) applies on or after June 19, 1996.

(iii) Section 1.475(b)–1(b)(3) (concerning certain actively-traded securities) generally applies on or after June 19, 1996, to securities held on or after that date. In the case, however, of securities described in § 1.475(b)–1(d)(1)(i) (concerning equity interests issued by controlled entities), § 1.475(b)–1(b)(3) applies on or after the date thirty days after final regulations on this subject are published in the **Federal Register** to securities held on or after that date. If § 1.475(b)–1(b)(1) ceases to apply to a security by virtue of the operation of this paragraph (d)(2)(ii), the rules of § 1.475(b)–1(b)(4)(ii) apply to the cessation.

(iv) Except to the extent provided in paragraph (d)(2)(i) of this section, § 1.475(b)–1(b)(4) (concerning changes in status) applies on or after Jun 19, 1996.

(e) Section 1.475(b)–2 (concerning the identification requirements for obtaining an exemption from mark-to-market treatment) applies to identifications made on or after January 4, 1995.

(f) Section 1.475(b)–3 (concerning exemption of securities in certain securitization transactions) applies to securities acquired, originated, or entered into on or after January 4, 1995.

(g) Section 1.475(b)–4 (concerning transitional issues relating to exemptions) applies to taxable years ending on or after December 31, 1993.

(h) Section 1.475(c)–1(a) (concerning the dealer-customer relationship), except for § 1.475(c)–1(a)(1), (a)(2)(ii), and (a)(3), applies to taxable years beginning on or after January 1, 1995. Section 1.475(c)–1(a)(2)(ii) and (a)(3) (concerning certain aspects of the dealer-customer relationship) apply to taxable years beginning on or after June 20, 1996.

(i) Section 1.475(c)–1(b) (concerning sellers of nonfinancial goods and services) and (c) (concerning taxpayers that purchase securities but do not sell more than a negligible portion of the securities) applies to taxable years ending on or after December 31, 1993.

(j) Section 1.475(c)–1(d) (concerning the issuance of life insurance products) applies to taxable years beginning on or after January 1, 1995.

(k) Section 1.475(c)–2 (concerning the definition of security) applies to taxable years ending on or after December 31, 1993. Note, however, that, by its terms, § 1.475(c)–2(a)(3) applies only to interests or arrangements that are acquired on or after January 4, 1995, and that the integrated transactions to which § 1.475(c)–2(b) applies will exist only after the effective date of § 1.1275–6.

(l) Section 1.475(d)–1 (concerning the character of gain or loss) applies to taxable years ending on or after December 31, 1993.

Margaret Milner Richardson,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on June 19, 1996, 8:45 a.m., and published in the issue of the Federal Register for June 20, 1996, 61 F.R. 31474)

Notice of Proposed Rulemaking and Notice of Public Hearing

Definition of Structure

PS–39–93

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations relating to deductions available upon demolition of a building. These proposed regulations reflect changes to the law made by the Tax Reform Act of 1984 and affect owners and lessees of real property who

demolish buildings. This document also provides notice of a public hearing on these regulations.

DATES: Written comments, requests to appear and outlines of topics to be discussed at the public hearing scheduled for October 9, 1996, must be received by September 19, 1996.

ADDRESSES: Send submissions to: CC:DOM:CORP:R (PS–39–93), room 5228, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. In the alternative, submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to: CC:DOM:CORP:R (PS–39–93), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the regulations, Bernard P. Harvey, (202) 622–3110; concerning submissions and the hearing, Christina Vasquez, (202) 622–6803 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed regulations under section 280B of the Internal Revenue Code. Section 280B was added by the Tax Reform Act of 1976, Public Law 94–455, 2124(b), 90 Stat. 1520, 1918 (Oct. 4, 1976), and significant amendments were made to the provision by the Economic Recovery Tax Act of 1981, Public Law 97–34, 212(d)(2)(C) and (e)(2), 95 Stat. 172, 239 (Aug. 13, 1981) (1981 Act) and the Tax Reform Act of 1984, Public Law 98–369, 1063, 98 Stat. 494, 1047 (July 18, 1984) (1984 Act). Transition rules were provided in the Tax Reform Act of 1986, Public Law 99–514, 1978(h), 100 Stat. 2085, 2904 (Oct. 22, 1986) (1986 Act). As originally enacted, section 280B required any costs or losses incurred on account of the demolition of any certified historic structure (a building or structure meeting certain requirements) to be capitalized into the land upon which the demolished structure was located. The 1981 Act modified the definition of certified historic structure for purposes of section 280B from a building or structure meeting certain requirements to a building (or its structural components) meeting certain requirements. The 1984 Act substituted "any structure" for "certified historic structure." These proposed regulations define what "structure" means for purposes of section 280B.

Explanation of Provisions

These proposed regulations define the term "structure" for purposes of section 280B as a building and its structural components as those terms are defined in § 1.48–1(e) of the Income Tax Regulations. Thus, under section 280B, a structure will include only a building and its structural components and not other inherently permanent structures such as oil and gas storage tanks, blast furnaces, and coke ovens.

The proposed regulations rely on the legislative history underlying the 1984 and 1986 Acts, which refer repeatedly to buildings rather than to structures generally. In addition, the legislative history of the 1984 Act discusses the difficulty of applying the intent test of § 1.165–3 of the regulations, which applies to the demolition of buildings, and indicates that the newly added language is meant to eliminate this difficulty.

Proposed effective date

The regulations are proposed to be effective on and after the date that final regulations are filed with the **Federal Register**.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure 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. Pursuant to section 7805(f) of the Internal Revenue Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written comments (a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be available for public inspection and copying.

A public hearing has been scheduled for October 9, 1996, in the Commissioner's Conference Room. Because of access restrictions, visitors will not be admitted beyond the Internal Revenue Building lobby more than 15 minutes before the hearing starts.

The rules of 26 CFR 601.601(a)(3) apply to the hearing.

Persons that wish to present oral comments at the hearing must submit written comments and an outline of the topics to be discussed and the time to be devoted to each topic (signed original and eight (8) copies) by September 18, 1996.

A period of 10 minutes will be allotted to each person for making comments.

An agenda showing the scheduling of the speakers will be prepared after the deadline for receiving outlines has passed. Copies of the agenda will be available free of charge at the hearing.

Drafting Information

The principal author of these regulations is Bernard P. Harvey, Office of Assistant Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

* * * * *

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 1.280B–1 is added to read as follows:

§ 1.280B–1 Demolition of structures.

(a) *In general.* Section 280B provides that, in the case of the demolition of any structure, no deduction otherwise allowable under chapter 1 of subtitle A shall be allowed to the owner or lessee of such structure for any amount expended for the demolition or any loss sustained on account of the demolition, and that the expenditure or loss shall be treated as properly chargeable to the capital account with respect to the land on which the demolished structure was located.

(b) *Definition of structure*. For purposes of section 280B, the term *structure* means a building, as defined in § 1.48–1(e)(1), and the structural components of that building, as defined in § 1.48–1(e)(2).

(c) *Effective date*. This section applies with respect to demolitions occurring on or after the date that the final regulations are filed with the **Federal Register**.

Margaret Milner Richardson,
Commissioner of Internal Revenue.

(Filed by the Office of the Federal Register on June 19, 1996, 8:45 a.m., and published in the issue of the Federal Register for June 20, 1996, 61 F.R. 31473)

Interest Netting Study

Announcement 96–75

SUMMARY: This announcement provides notice that a public hearing will be held in connection with a study of "global interest netting" being conducted by the Internal Revenue Service and Treasury. Notice 96–18, 1996–14 I.R.B. 27 (April 1, 1996), described a number of legal and policy issues arising from global interest netting, as well as administrative concerns relating to the Service's computer system capability to implement global interest netting. Notice 96–18 invited public comment on these issues and requested that written comments be submitted by June 30, 1996.

DATES: The public hearing will be held on Wednesday, September 4, 1996, beginning at 10:00 a.m. Requests to speak and outlines of oral comments must be received by August 30, 1996.

ADDRESSES: The public hearing will be held in Room 2615 of the Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20044. Requests to speak and outlines of oral comments should be submitted either by mail to:

Internal Revenue Service
P.O. Box 7604, Ben Franklin Station
Attn: CC:DOM:CORP:T:R:IT&A
(Branch 1), Room 5228
Washington, D.C. 20044,

or electronically via the Service Internet site at:
http://www.irs.ustreas.gov/prod/tax_regs/comments.html.

FOR FURTHER INFORMATION CONTACT: Christina Vasquez of the Regulations Unit, Assistant Chief Counsel (Corporate), (202) 622–6808 (not a toll-free call).

SUPPLEMENTARY INFORMATION:

The subject of the public hearing is the legal, policy, and administrative issues relating to global interest netting. In addition, the Service and Treasury request that persons who speak at the hearing be prepared to discuss examples of situations in which global interest netting would be appropriate.

Persons who wish to speak at the hearing should submit, not later than August 30, 1996, an outline of the oral comments/testimony to be presented at the hearing and the time they wish to devote to each subject.

Each speaker (or group of speakers representing a single entity) will be limited to 10 minutes for an oral presentation exclusive of the time consumed by the questions from the panel for the government and the answers thereto.

Because of controlled access restrictions, attendees cannot be admitted beyond the lobby of the Internal Revenue Building until 9:45 a.m.

An agenda showing the scheduling of the speakers will be made after the outlines are received from the persons testifying. Copies of the agenda will be available free of charge at the hearing.

Rev. Proc. 96–36; Correction

Announcement 96–76

This announcement is a correction to Rev. Proc. 96–36, 1996–27 I.R.B. 11, which provides specifications for filing Forms 1098, 1099, 5498, and W–2G. The final page of the document was omitted. This label page is referred to in Part A, Section 9.11 and should have appeared in Part F, Section 3.

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This is the end of Publication 1220 for Tax Year 1996.

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with *modified*, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with *amplified* and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in law or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in the new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, *modified* and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.

Acq.—Acquiescence.

B—Individual.

BE—Beneficiary.

BK—Bank.

B.T.A.—Board of Tax Appeals.

C.—Individual.

C.B.—Cumulative Bulletin.

CFR—Code of Federal Regulations.

CI—City.

COOP—Cooperative.

Ct.D.—Court Decision.

CY—County.

D—Decedent.

DC—Dummy Corporation.

DE—Donee.

Del. Order—Delegation Order.

DISC—Domestic International Sales Corporation.

DR—Donor.

E—Estate.

EE—Employee.

E.O.—Executive Order.

ER—Employer.

ERISA—Employee Retirement Income Security Act.

EX—Executor.

F—Fiduciary.

FC—Foreign Country.

FICA—Federal Insurance Contribution Act.

FISC—Foreign International Sales Company.

FPH—Foreign Personal Holding Company.

F.R.—Federal Register.

FUTA—Federal Unemployment Tax Act.

FX—Foreign Corporation.

G.C.M.—Chief Counsel's Memorandum.

GE—Grantee.

GP—General Partner.

GR—Grantor.

IC—Insurance Company.

I.R.B.—Internal Revenue Bulletin.

LE—Lessee.

LP—Limited Partner.

LR—Lessor.

M—Minor.

Nonacq.—Nonacquiescence.

O—Organization.

P—Parent Corporation.

PHC—Personal Holding Company.

PO—Possession of the U.S.

PR—Partner.

PRS—Partnership.

PTE—Prohibited Transaction Exemption.

Pub. L.—Public Law.

REIT—Real Estate Investment Trust.

Rev. Proc.—Revenue Procedure.

Rev. Rul.—Revenue Ruling.

S—Subsidiary.

S.P.R.—Statements of Procedural Rules.

Stat.—Statutes at Large.

T—Target Corporation.

T.C.—Tax Court.

T.D.—Treasury Decision.

TFE—Transferee.

TFR—Transferor.

T.I.R.—Technical Information Release.

TP—Taxpayer.

TR—Trust.

TT—Trustee.

U.S.C.—United States Code.

X—Corporation.

Y—Corporation.

Z—Corporation.

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[1] A cumulative list of all Revenue Rulings, Revenue Procedures, Treasury Decisions, etc., published in Internal Revenue Bulletins 1996–1 through 1996–26 will be found in Internal Revenue Bulletin 1996–27, dated July 1, 1996.

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[1]A cumulative finding list for previously published items mentioned in Internal Revenue Bulletins 1996–1 through 1996–26 will be found in Internal Revenue Bulletin 1996–27, dated July 1, 1996.