

Limitations for 2008” in Notice 2008–107 should use the amounts found in that table (which can also be found in the Instructions to Form 2555 (2009)) to determine their adjusted limitation for 2009.

## SECTION 5. ELECTION TO APPLY 2010 ADJUSTED LIMITATIONS TO 2009 TAXABLE YEAR

For some locations, the limitation on housing expenses provided in section 3 of this notice may be higher than the limitation on housing expenses provided in the “Table of Adjusted Limitations for 2008” in Notice 2008–107. A qualified individual incurring housing expenses in such a location during 2009 may apply the adjusted limitation on housing expenses provided in section 3 of this notice in lieu of the amounts provided in the “Table of Adjusted Limitations for 2008” in Notice 2008–107 (and as set forth in the Instructions to Form 2555 (2009)).

Treasury and the IRS anticipate that future annual notices providing adjustments to housing expense limitations will make a similar election available to qualified individuals that incur housing expenses in the immediately preceding year. For example, when adjusted housing expense limitations for 2011 are issued, it is expected that taxpayers will be permitted to apply those adjusted limitations to the 2010 taxable year.

## EFFECT ON OTHER DOCUMENTS

This notice supersedes Notice 2006–87, 2006–2 C.B. 766, Notice 2007–25, 2007–1 C.B. 760, Notice 2007–77, 2007–2 C.B. 735, and Notice 2008–107, 2008–50 I.R.B. 1265.

## EFFECTIVE DATE

This notice is effective for taxable years beginning on or after January 1, 2010. However, as provided in section 5, a taxpayer may elect to apply the 2010 adjusted housing limitations contained in section 3 of this notice to his or her taxable year beginning in 2009.

## DRAFTING INFORMATION

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# Stripping Transactions for Qualified Tax Credit Bonds

## Notice 2010–28

### SECTION 1. INTRODUCTION

This notice describes regulations that the Treasury Department and the Internal Revenue Service (IRS) expect to issue concerning both stripping transactions for qualified tax credit bonds under section 54A of the Internal Revenue Code and certain income tax accounting matters associated with holding and stripping these bonds. Pending the promulgation and effective date of future administrative or regulatory guidance, this notice provides interim guidance on which taxpayers may rely. In addition, this notice describes anticipated related information reporting requirements and solicits public comments on the interim guidance and the information reporting requirements.

### SECTION 2. BACKGROUND

Section 54A(a) provides that a taxpayer that holds a qualified tax credit bond on one or more credit allowance dates during any taxable year is allowed a tax credit for such year in an amount equal to the sum of the credits determined under section 54A(b) with respect to such dates.

Section 54A(d)(1) defines a qualified tax credit bond to include the following types of bonds if they meet applicable requirements: (1) qualified forestry conservation bonds, (2) new clean renewable energy bonds, (3) qualified energy conservation bonds, (4) qualified zone academy bonds, and (5) qualified school construction bonds.

Section 54A(e)(1) provides that the credit allowance dates for a qualified tax credit bond are March 15, June 15, September 15, and December 15 of any year in which the bond is outstanding and the last day on which the bond is outstanding.

Under section 54A(b)(2), the annual credit on a qualified tax credit bond is the product of the applicable credit rate

multiplied by the outstanding face amount of the bond. Subject to special rules in section 54A(b)(4) for short periods, section 54A(b)(1) provides that the amount of credit for any credit allowance date is 25 percent of the annual credit on a qualified tax credit bond.

For holders of new clean renewable energy bonds and qualified energy conservation bonds, section 54C(b) and section 54D(b) limit the amount of the annual credit otherwise determined under section 54A(b) to 70 percent of the amount so determined without regard to section 54C(b) and section 54D(b).

Section 54A(c)(1) generally provides that the credit allowed under section 54A(a) for any taxable year may not exceed the excess of (1) the sum of the regular and the alternative minimum tax liability of the taxpayer, over (2) the sum of certain allowable credits. Under section 54A(c)(2), unused excess credits may be carried forward for use in succeeding taxable years.

Section 54A(f) provides that, for Federal income tax purposes, the credit determined under section 54A(a) is treated as interest that is includible in gross income.

Section 54A(i)(1) provides that, under regulations prescribed by the Secretary, there may be a separation (including at issuance) of the ownership of a qualified tax credit bond and the entitlement to the credit with respect to that bond. Section 54A(i)(1) further provides that, in case of any such separation, the credit under section 54A is allowed to the person who on the credit allowance date holds the instrument evidencing the entitlement to the credit and not to the holder of the bond. Section 54A(i)(2) further provides that, in the case of any such separation, the rules of section 1286 are to apply to the qualified tax credit bond as if it were a stripped bond and to the credit under section 54A as if it were a stripped coupon.

### SECTION 3. INTERIM GUIDANCE AND RELIANCE

#### .01 IN GENERAL

Sections 3.02 and 3.03 of this notice describe the substance of regulations that the IRS and the Treasury Department expect to issue. Pending the promulgation and effective date of future administrative

or regulatory guidance, this notice provides interim guidance on which taxpayers may rely with respect to qualified tax credit bonds issued under section 54A. For further information regarding the effective date and scope of application, see Section 7 of this notice.

## .02 QUALIFIED TAX CREDIT BONDS—TREATMENT OF THE CREDIT BY HOLDERS

(a) *Allowance of credit*—(1) *General rule.* In general, a taxpayer that holds a qualified tax credit bond on one or more credit allowance dates (as defined in section 54A(e)(1)) of the bond occurring during a taxable year is allowed as a credit against income tax for the taxable year an amount equal to the sum of the credits determined under section 54A(b) with respect to those credit allowance dates. Unless otherwise specifically provided, for purposes of this notice references to the “allowance of a credit” or an “allowed credit” mean the amount of the credit determined under section 54A(b) (as limited by sections 54C(b) and 54D(b)) before application of the limitation under section 54A(c).

(2) *Allowance of a credit treated as a payment of stated interest on a taxable bond.* For Federal income tax purposes, the allowance of a credit on a qualified tax credit bond on a credit allowance date is treated as a payment, in the amount of the allowed credit, of stated interest on a debt obligation the interest on which is includable in gross income. Thus, the allowance of a credit on a bond that has not undergone a stripping transaction is treated as a payment of qualified stated interest (within the meaning of § 1.1273-1(c) of the Income Tax Regulations) to the same extent that a payment of stated interest in cash in the same amount and on the same date would have been so treated.

(3) *Accounting method*—(i) *General rule.* In general, a holder’s regular method of accounting determines when the holder recognizes qualified stated interest income from a qualified tax credit bond. Thus, if the holder of a qualified tax credit bond uses the cash receipts and disbursements method of accounting, interest income in the amount of the allowed credit is generally included in income on the credit allowance date. If the holder of such a

bond uses an accrual method of accounting, this interest income is included in income as it accrues over each accrual period. See § 1.1272-1(b)(1)(ii) to determine the accrual periods and § 1.446-2(b) to determine how qualified stated interest accrues over the accrual period (or periods) to which it is attributable. (For qualified tax credit bonds that have not undergone a stripping transaction, because of the regular quarterly credit allowance dates, the maximum permitted length of the accrual periods is three months.)

(ii) *Other rules with respect to accounting for interest.* Under certain circumstances, other rules may require the holder of a bond (including a tax credit bond) to adjust the amount of interest income that the holder recognizes. See, e.g., section 171 (amortization of bond premium by a bond purchaser); § 1.61-7(c) (purchaser’s treatment of a bond purchased between interest payment dates); § 1.61-7(d) (seller’s treatment of a bond sold between interest payment dates); section 1272 (accrual of original issue discount (OID) by a holder); and Section 3.03 of this notice and section 1286 (treatment of stripping transactions).

(4) *Examples.* The following examples illustrate the application of this Section 3.02(a):

*Example 1.* Assume that, on December 15, 2011, City X issues a qualified tax credit bond with a stated principal amount of \$12,000, a credit rate of 10% compounded quarterly, and a maturity date of December 15, 2013. B purchases the bond at original issue for \$12,000 and thus has a \$12,000 basis in the bond. B is a calendar year taxpayer that uses the cash receipts and disbursements method of accounting. Under Section 3.02(a) of this notice and § 1.1273-1(c), the allowance of the \$300 tax credit on each credit allowance date is treated as a payment of qualified stated interest of \$300 on those dates. On March 16, 2012, B sells the bond for \$12,000. On March 15, 2012, the first credit allowance date occurring after the issuance of the bond, B becomes entitled to a \$300 tax credit and, with respect to that credit, must include in income \$300 of interest in 2012. No interest is includable in 2011.

*Example 2.* The facts are the same as in *Example 1*, except that B uses an accrual method of accounting. As in *Example 1*, B becomes entitled to a \$300 tax credit on March 15, 2012. B, however, must include in income \$50 of interest in 2011 and \$250 of interest in 2012 (based on a 30 day/360 day counting convention).

*Example 3*—(i) The facts are the same as in *Example 1*, except that on March 16, 2012, B sells the bond for \$12,100 to C, a taxpayer that uses the cash receipts and disbursements method and the calendar year. C has not previously elected to amortize bond premium under section 171. Under § 1.61-7(d), B treats the entire \$12,100 as sales proceeds. Because

B’s basis in the bond was \$12,000, B has a \$100 gain on the sale. C has a \$12,100 basis in the bond. Because C acquired the bond with premium of \$100, C may elect to amortize the \$100 bond premium under section 171.

(ii) Assume further that C holds the bond until its retirement on December 15, 2013. C has \$900 of tax credits in 2012 and \$1,200 in 2013. If C does not elect to amortize the bond premium, C has \$900 of interest income in taxable year 2012 and \$1,200 of interest income in taxable year 2013. In addition, C has a \$100 loss in taxable year 2013. If C elects to amortize the \$100 of bond premium, the amortized portion of that bond premium reduces C’s interest income in 2012 and 2013, and C does not have a \$100 loss in taxable year 2013.

*Example 4.* The facts are the same as in *Example 3*, except that B sells the bond to C on January 15, 2012, at a sales price of \$12,100. (Based on the treatment of the credits under section 3.02(a)(2) of this notice, there was \$100 of accrued but unpaid interest with respect to the bond on the sale date.) Under § 1.61-7(d), B treats \$100 of the sales price as the receipt of interest accrued on the bond, includes this amount in income in 2012, and treats the remaining \$12,000 as sales proceeds. Because B’s basis in the bond is \$12,000, B has no gain or loss on the sale of the bond. On March 15, 2012, C becomes entitled to the \$300 credit. Under § 1.61-7(c), the amount of interest income included by C with respect to the credit is \$200, and C’s basis in the bond is \$12,000.

(b) *Limitation based on amount of tax*—(1) *In general.* The credit allowed under section 54A(a) and this Section 3.02 is subject to the limitation in section 54A(c)(1) based on the taxpayer’s income tax liability.

(2) *Carryover of unused credit*—(i) *In general.* Under section 54A(c)(2), if the credit allowable for the taxable year under section 54A(a) exceeds the limitation imposed for the taxable year by section 54A(c)(1), the excess credit (an excess credit) is carried to the succeeding taxable year and added to the credit allowable under section 54A(a) (as adjusted by sections 54C(b) and 54D(b)) for the succeeding taxable year (determined before the application of the limitation for the succeeding taxable year under section 54A(c)(1)).

(ii) *No time limit on carryovers of excess credits.* An excess credit under section 54A(c)(2) can be carried forward to succeeding taxable years and used in a succeeding year to the extent that the excess credit does not exceed the limitation for that taxable year. Any allowed credit, including any excess credit from a prior year, however, must be taken for the first taxable year in which, and to the extent that, the allowed credit, including the excess credit, does not exceed the limitation under sec-

tion 54A(c)(1) and Section 3.02(b)(2)(i) of this notice.

(c) *Qualified tax credit bonds and corporate earnings and profits*—(1) *Adjustments to earnings and profits*. A corporation generally adjusts its earnings and profits in accordance with its method of accounting. See § 1.312–6. For this purpose, a corporation increases its earnings and profits for interest income (including interest described in section 54A(f)). A corporation reduces its earnings and profits when, and to the extent that, it would have reduced its earnings and profits had it satisfied its tax liability with cash rather than reducing that liability with tax credits from qualified tax credit bonds.

(2) *RICs and REITs*. If, under section 853A or section 54A(h), a regulated investment company or a real estate investment trust, respectively, distributes with respect to its stock a tax credit from a qualified tax credit bond or from a stripped credit coupon from a qualified tax credit bond (including a credit passed through from a partnership or trust), then the earnings and profits of the regulated investment company or real estate investment trust are reduced when, and to the extent that, the earnings and profits would have been reduced if the distribution had consisted of cash in the amount of the credit.

### .03 QUALIFIED TAX CREDIT BONDS—TREATMENT OF STRIPPING TRANSACTIONS

(a) *Overview*. This Section 3.03 addresses stripping transactions involving qualified tax credit bonds. Section 54A(i)(1) provides generally that, under regulations, there may be a separation, including at issuance, of the ownership of a qualified tax credit bond and the entitlement to a credit under section 54A with respect to the bond. In the case of any such separation, the credit is allowed to the person who on the credit allowance date holds the instrument evidencing the entitlement to the credit and not to the holder of the bond. Section 54A(i)(2) further provides that, in the case of such a separation, the rules of section 1286 are to apply to the qualified tax credit bond as if it were a stripped bond and to the credit as if it were a stripped coupon.

(b) *Definitions*. The following definitions apply for purposes of this Section 3:

(1) *Credit coupon* means the right to receive a tax credit under section 54A with respect to a qualified tax credit bond on a credit allowance date.

(2) *Issue* means issue as defined in § 1.150–1(c) except that, in applying that definition for purposes of this Section 3.03, the only bonds taken into account are qualified tax credit bonds as defined in section 54A(d)(1).

(3) *Stripping transaction* means a transaction that results in the separation in ownership between any credit coupon with respect to a qualified tax credit bond for any credit allowance date that has not yet occurred and any right to receive cash (whether stated principal or stated interest) that has not yet become payable. Notwithstanding the preceding sentence, the term stripping transaction does not include a transaction with respect to a particular bond in which the post-transaction future rights (that is, rights to cash that is not yet payable and credits whose credit allowance dates have not yet occurred) reflect a *pro rata* division of all the pre-transaction future rights.

(4) *Stripped credit coupon* means a credit coupon with respect to a qualified tax credit bond if the bond has undergone a stripping transaction.

(c) *Strippable Issue*. For purposes of this notice, the term “strippable issue” means an issue of qualified tax credit bonds that complies with all of the following requirements:

(1) *Designation requirement*. The issuer on or before the date of issue includes a statement in the bond documents (as defined in § 1.150–1(b)) that the issue of qualified tax credit bonds is strippable. For an issue of qualified tax credit bonds that is issued before March 31, 2010, this designation may be effected on or before May 17, 2010.

(2) *Identification requirement*. On an information return filed with the IRS under section 54A(d)(3), the issuer identifies the issue of qualified tax credit bonds as a strippable issue. Except as provided in the next sentence, the identification must be on the first information return filed under section 54A(d)(3) with respect to the issue of qualified tax credit bonds. For an issue of qualified tax credit bonds that is issued before March 31, 2010, the identification may instead be on an amended information return filed before May 17, 2010.

(3) *Registration requirement*. The issue of qualified tax credit bonds is issued in registered form. For this purpose, registered form means that all rights to stated principal, stated cash interest, and tax credits under the bond may be transferred only through book entry on the registration books of the issuer or an agent or nominee (or chain of nominees) for this purpose. In addition, a bond is not considered to be in registered form unless book entries are maintained (by the issuer, an agent, or nominee) in a manner that makes all the entries available for inspection upon request by the Commissioner or his designees.

(4) *CUSIP number requirement*. A CUSIP number is assigned to the issue of qualified tax credit bonds, a separate CUSIP number is assigned to all rights to receive tax credits on each credit allowance date with respect to the issue, and at least one separate CUSIP number is assigned to all rights to receive cash (whether stated principal or stated interest) with respect to the issue.

(d) *Allowance of the tax credit to a holder of a stripped credit coupon*. A taxpayer who holds a stripped credit coupon on a credit allowance date is allowed the tax credit only if all of the following requirements are satisfied:

(1) *Strippable issue*. The bond is part of a strippable issue within the meaning of paragraph (c) of this Section 3.03.

(2) *Stripped credit coupons*. The stripped credit coupon is either a whole credit coupon or a proportional share of a whole credit coupon. Thus, if a person holds any other division of a whole credit coupon, including any direct or indirect division or modification of a whole credit coupon effected through a partnership, trust, or other investment arrangement that, in substance, causes the person to hold a variable share of the whole credit coupon, then no tax credit is allowed with respect to that interest in the credit coupon. For example, if a person holds an interest in a partnership or a share of a trust that effects any division of a whole credit coupon held by the partnership or trust other than a proportional division, then that person (and any other person to whom the person directly or indirectly passes the credit) is not entitled to a tax credit with respect to the person’s allocable share or beneficial

interest in that division of the whole credit coupon.

(3) *Broker accounts.* The taxpayer holds the stripped credit coupon in an account with—

(i) A broker as defined in section 6045(c)(1); or

(ii) Any other person to the extent provided by the Commissioner in published guidance.

(e) *Treatment of a stripping transaction involving a qualified tax credit bond—(1) In general.* Except to the extent that a provision of this Section 3.03 explicitly provides otherwise, subsections (a), (b), and (e) of section 1286 apply to stripping transactions involving qualified tax credit bonds. In applying these provisions of section 1286, the allowance of a credit is treated in the same manner as a cash payment of stated interest on the credit allowance date. See Section 3.02(a)(2) of this notice.

(2) *Aggregation and other rules.* If, on a single date, a taxpayer purchases (including a purchase under section 1286(b)(4)), as part of a single transaction or series of related transactions, more than one component (stated principal, stated cash interest, or credit coupons) of a qualified tax credit bond that has been subject to a stripping transaction, then, for purposes of sections 1271 through 1286 and the regulations thereunder, the taxpayer must treat the components so purchased as a single debt instrument (the aggregated debt instrument) that was newly issued on the purchase date. Notwithstanding the prior sentence, none of the payments on the aggregated debt instrument is treated as qualified stated interest under § 1.1273-1(c). If, in a manner described in the first sentence of this Section 3.03(e)(2), the taxpayer purchases all of the then-outstanding components of a qualified tax credit bond, then the resulting aggregated debt instrument is treated as of the purchase date as if it had not been subject to a previous stripping transaction, and thus the second sentence of this Section 3.03(e)(2) does not apply.

(f) *Examples.* The rules in this Section 3.03 are illustrated by the following examples.

*Example 1—(i) Facts.* On December 15, 2011, City X issues an issue of qualified school construction bonds as a single bond with a stated principal amount

of \$12,000, a credit rate of 10% compounded quarterly, and a maturity date of December 15, 2013. Assume that none of the interest on the bond is payable in cash. (That is, there is no supplemental cash interest coupon.) X, on or before the date of issue, includes in the bond documents a statement that the issue is stripable and issues the issue in registered form. X obtains 10 CUSIP numbers with respect to the issue (1 CUSIP number for the \$12,000 issue of qualified school construction bonds, a separate CUSIP for the credit coupons for each of the 8 credit allowance dates through the scheduled maturity of the issue, and 1 CUSIP number for the scheduled principal payment at maturity). On the first information return that X files with the IRS with respect to this issue under section 54A(d)(3), X indicates that the issue is a stripable issue of qualified school construction bonds.

(ii) *Analysis.* X's issue of qualified school construction bonds is a stripable issue because it satisfies the requirements of Section 3.03(c)(1) through (4) of this notice.

*Example 2.* The facts are the same as in *Example 1*, except that, on December 15, 2011, X sells the \$12,000 bond to Y. Y sells on December 15, 2011, a \$6,000 *pro rata* portion of the bond to A, a cash method, calendar year taxpayer, and a \$6,000 *pro rata* portion of the bond to B, an accrual method, calendar year taxpayer. (Thus, Y's sales to A and B do not constitute a stripping transaction, because they effect a *pro rata* division of the future rights under the bond.) The purchase prices paid by A and B were \$6,000 each. On March 15, 2012 (and all subsequent credit allowance dates), subject to the limitations contained in section 54A(c)(1) and Section 3.02(b)(1) of this notice, A and B are each entitled to claim a \$150 tax credit.

*Example 3—(i) Facts.* The facts are the same as in *Example 2*, except that, on December 15, 2011, A sells the December 15, 2013, credit coupon of \$150 to C, a cash method calendar year taxpayer for \$123.75 (its fair market value). After the sale, A holds the right to receive \$6,000 at maturity as well as the first 7 credit coupons (the "8 retained components"), and C holds only the December 15, 2013, credit coupon.

(ii) *Application of definitions.* The sale is a stripping transaction within the meaning of Section 3.03(b)(3) of this notice. The credit coupon held by C and the 7 credit coupons retained by A are all stripped credit coupons. The treatment of B's bond is not affected by the sale.

(iii) *A's treatment of the sale.* Under Section 3.03(e)(1) of this notice, section 1286(b) applies to this stripping transaction. Section 1286(b)(4) treats A as having purchased the 8 retained components on the date on which A sells the December 15, 2013, credit coupon to C. Under Section 3.03(e)(2) of this notice, the 8 retained components must be treated as an aggregated debt instrument that is newly issued on the date of the sale of that credit coupon.

Prior to the sale of the credit coupon, A's basis in the unstripped \$6,000 bond is A's purchase price of \$6,000. Because no interest is treated as having accrued on the bond prior to the sale, A is not required to include an amount in income under section 1286(b)(1)(A), and thus no amount needs to be added to A's basis under section 1286(b)(2). Pursuant to section 1286(b)(3), A must allocate its basis in the

bond (\$6,000) between the credit coupon that A sold and A's aggregated debt instrument, based on their respective fair market values. Assume that, on the date of the sale, the fair market value of A's aggregated debt instrument is \$5,877.10 and the fair market value of the December 15, 2013, credit coupon sold by A is \$123.75 (total fair market value of \$6,000.85). Based on these fair market values, A's basis in the aggregated debt instrument is \$5,876.27 (\$6,000 basis x [\$5,877.10 / \$6,000.85]) and A's basis in the December 15, 2013, credit coupon is \$123.73 (\$6,000 basis x [\$123.75 / \$6,000.85]). As a result, A realizes a gain of \$0.02 on the sale of the December 15, 2013, credit coupon (amount realized of \$123.75, minus basis of \$123.73).

(iv) *A's treatment of the aggregated debt instrument.* Under section 1286(b)(4), A is treated as purchasing the aggregated debt instrument for \$5,876.27. The purchase is treated as taking place on the date of the sale to C, and the purchase price is equal to the portion (\$5,876.27) of A's \$6,000 basis that is allocated to the aggregated debt instrument. Under Section 3.03(e)(2) of this notice, A must treat the aggregated debt instrument as newly issued on that date for \$5,876.27. Thus, the aggregated debt instrument has an issue price of \$5,876.27. Under Section 3.03(e)(2) of this notice, no payment on the aggregated debt instrument is qualified stated interest under § 1.1273-1(c). As a result, the stated redemption price at maturity of the aggregated debt instrument is \$7,050 (\$6,000 + [7 x \$150]). The aggregated debt instrument, therefore, has OID of \$1,173.73 (\$7,050 - \$5,876.27). Although A generally uses the cash receipts and disbursements method of accounting, A must include the OID in income as it accrues on a constant yield basis over the term of the aggregated debt instrument in accordance with section 1272 and the regulations thereunder.

(v) *C's treatment of the stripped tax credit coupon.* Under Section 3.03(e)(1) of this notice, section 1286(a) applies to C's purchase of the December 15, 2013, stripped credit coupon. Section 1286(a) requires C to treat the purchase of this stripped credit coupon as the purchase of a zero coupon bond that is issued on the date of purchase (December 15, 2011). The stripped credit coupon has a stated redemption price at maturity of \$150 and an issue price of \$123.75, resulting in OID of \$26.25 (\$150 - \$123.75). The term of the stripped credit coupon begins on December 15, 2011, and ends on December 15, 2013. Although C generally uses the cash receipts and disbursements method of accounting, C must include the OID in income as it accrues on a constant yield basis over that term in accordance with section 1272 and the regulations thereunder.

C's basis in the stripped credit coupon is increased by the amount of OID that is included in C's income. As a result, C's basis in the stripped credit coupon on the December 15, 2013, credit allowance date will be \$150. On that date, C will become entitled to the \$150 of credit. Thus, C does not have any gain or loss when the coupon matures and C becomes entitled to the \$150 tax credit.

## **SECTION 4. INFORMATION REPORTING REQUIREMENTS RELATED TO TAX CREDIT BONDS**

### **.01 IN GENERAL**

Qualified tax credit bonds—in particular, stripping transactions involving these bonds—raise significant tax compliance and tax administration issues. The Treasury Department and the IRS plan to implement and maintain a robust system of information reporting in this area to facilitate tax compliance and strengthen tax administration.

Section 54A(d)(3) requires issuers of qualified tax credit bonds to submit information reports regarding the bonds similar to the reports required under section 149(e).

Section 6049(d)(9)(A) provides that, for purposes of the information reporting requirements under section 6049(a) regarding payments of interest, the term interest includes amounts includible in gross income under section 54A, and those amounts are treated as paid on the credit allowance date.

Under section 6049(d)(6), section 6049(a) generally requires OID on any obligation to be reported as if it were paid at the time that the OID is includible in income under section 1272. This provision governs section 6049 information reporting when a tax credit under a qualified tax credit bond is included in an instrument's stated redemption price at maturity, and thus contributes to OID. (This occurs when the allowance of the credit is not treated as a payment of qualified stated interest on an instrument, for example, when a stripped credit coupon is part of an aggregated debt instrument that is subject to the second sentence of Section 3.03(e)(2) of this notice.)

Section 6049(b)(2)(B)(i) and section 6049(b)(4) generally exempt from information reporting interest that is paid to certain persons. Section 6049(d)(9)(B), however, generally makes this exemption inapplicable for interest on qualified tax credit bonds that is treated as paid to the following entities: (i) corporations; (ii) dealers in securities or commodities required to register under the laws of the United States, any State, the District of Columbia or any United States possession; (iii) real estate investment trusts

(as defined in section 856); (iv) entities registered at all times during the taxable year under the Investment Company Act of 1940; (v) common trust funds (as defined in section 584(a); and (vi) trusts exempt from tax under section 664(c). Notwithstanding the preceding sentence, the exemption continues to apply to interest that is covered by an express regulatory exception.

Section 6049(d)(9)(C) provides broad authority to the Treasury Department to issue regulations as necessary or appropriate to carry out the purposes of section 6049(d)(9), including regulations that require more frequent or more detailed reporting.

The Treasury Department and the IRS will attempt to ensure that both the IRS and investors receive accurate information about interest income (including OID) that is includable in income as a result of holding qualified tax credit bonds and components stripped from these bonds. The Treasury Department and the IRS will also seek to ensure that tax credits from qualified tax credit bonds (including tax credits from stripped credit coupons) are claimed only when the claimant is entitled to those credits.

To these ends, the Treasury Department and the IRS anticipate implementing the integrated system of information reporting that is described below in this Section 4. This may involve implementing new requirements. Revised forms and, if necessary, regulations will be issued to implement these information reporting requirements. For example, when a taxpayer holds a stripped credit coupon in an account with a broker as defined in section 6045(c)(1) (see Section 3.03(d)(3) of this notice), future guidance is expected to require the broker to compute, and report to the holder of the stripped credit coupon and to the IRS, the OID that accrues on that coupon under Section 3.03(e) of this notice and section 1286(a)-(b).

This system of information reporting will be subject to the same penalties that apply generally with respect to the failure to accurately file required forms. These include but are not limited to the penalties under sections 6049, 6721, and 6722 (which are applied to issuers, issuers' agents, and independent intermediaries) and the penalty under section 6694 and

Rev. Proc. 2009-11, 2009-3 I.R.B. 313 (which is applied to paid preparers).

As the forms and instructions to be used to implement the integrated information reporting system become available for use or for review in draft form, the IRS plans to publish them on its web site at <http://www.irs.gov/app/picklist/list/formsInstructions.html> and <http://www.irs.gov/app/picklist/list/draft-TaxForms.html>, respectively. Taxpayers wishing to provide comments to the IRS on draft tax forms can do so on the IRS web site at <http://www.irs.gov/formspubs/page/0,,id=10179,00.html>.

### **.02 INFORMATION RETURNS UNDER SECTION 54A(d)(3)**

Section 54A(d)(3) requires issuers of qualified tax credit bonds to file information returns. Although Form 8038 is now used for this purpose, the IRS intends to publish a new form (Form 8038-TC) to be used in this situation. As is provided by Section 3.03(c)(2) of this notice, the issuer of a strippable issue is now required, as part of this reporting obligation, to identify the issue as a strippable issue and to provide all of the CUSIP numbers that Section 3.03(c)(4) of this notice requires. Issuers must provide this information on Form 8038 or an attachment thereto until the new Form 8038-TC becomes available and thereafter on this new form.

### **.03 REPORT OF A TAXPAYER CLAIMING A TAX CREDIT ON AN INCOME TAX RETURN**

If a taxpayer claims on its income tax return a tax credit authorized by section 54A, the taxpayer is required to include Form 8912 as part of the return. The IRS and Treasury Department anticipate that the information required on this form will be modified to include not only the type of tax credit bond and the amount of credit claimed but also the tax identification number of the issuer of the bond and the CUSIP number for the qualified tax credit bond (or the stripped credit coupon) that is the basis of the credit being claimed.

### **.04 TAX CREDIT ALLOWANCE INFORMATION RETURN**

Under section 6049, the IRS expects to publish a new form, Form 1097-BTC, to

inform both the IRS and any recipient of a credit under section 54A of the amount of the tax credit that the credit recipient has received for each credit allowance date. The amount to be reported is the amount of the allowed credit to which the recipient is entitled within the meaning of Section 3.02(a)(1). It is anticipated that this form will be used in two distinct situations. First, it will have to be filed by, or on behalf of, the issuer. Second, a filing will also be required of each broker or intermediary that is not acting on behalf of the issuer (an independent intermediary).

As for the issuer requirement, the principles under section 6049(d)(4) are expected to apply to limit this requirement to the last responsible person or intermediary acting on behalf of the issuer.

The requirement for independent intermediaries is expected to apply whenever such an intermediary serves as an agent or nominee with respect to a credit or the intermediary receives a credit and passes it on either to another independent intermediary or to the taxpayer that will ultimately claim the credit. (Examples of independent intermediaries include a broker that is not reporting on behalf of the issuer, a partnership, a trust, an estate, and a regulated investment company or real estate investment trust that distributes tax credits with respect to its stock under section 853A or section 54A(h)).

It is anticipated that this form will operate in the following fashion—

- The information required by the form will include not only the amount of the credit transferred to the recipient but also the bond issuer's tax identification number and the CUSIP number for the qualified tax credit bond (or stripped credit coupon) that is the basis for the credit being transmitted.
- Effective starting with credits received in 2010, responsible persons under section 6049 will be required to submit a form to the IRS annually after the close of the calendar year. The form will include the total amount of tax credits for which the responsible persons served as a responsible person during the taxable year with respect to each independent intermediary and each holder of a tax credit bond or stripped credit coupon. The form will

require the CUSIP number of the bond (or the stripped credit coupon) generating that tax credit and the tax identification number of the issuer of the bond that underlies the tax credit.

- Effective starting with credits received in 2011, responsible persons under section 6049 will be required to send this form to the credit recipient quarterly within 30 to 60 days following the credit allowance date to which the tax credit relates.
- The form will require that the entity generating the form indicate whether the entity is the bond issuer (including a person acting on behalf of the bond issuer) or whether it is an independent intermediary and thus is not only the generator of a form but also the recipient of such a form from another independent intermediary or from the bond issuer (including a person acting on behalf of the bond issuer).

#### .05 REPORT FOR INCOME FROM INTEREST, ORIGINAL ISSUE DISCOUNT, OR DIVIDENDS

(a) For qualified tax credit bonds, information reporting for interest and OID under section 6049 will be expanded. Responsible persons under section 6049 will generally be required annually to provide the IRS and the holder of a qualified tax credit bond or stripped credit coupon with an information return indicating the amount of interest income paid (or treated as paid for purposes of section 6049) to the holder during that annual period with respect to any qualified tax credit bond. As stated above, when a taxpayer holds a stripped credit coupon in an account with a broker as defined in section 6045(c)(1) (see Section 3.03(d)(3) of this notice), future guidance is expected to require the broker to compute, and report, the OID on that coupon that accrues under Section 3.03(e) of this notice and section 1286(a)-(b). An analogous requirement may apply to any other stripped component from a qualified tax credit bond.

(b) It is expected that if a regulated investment company or a real estate investment trust receives tax credits allowed by section 54A (either because it holds a qualified tax credit bond or stripped coupon or because it received the credits from an

independent intermediary) and distributes with respect to its stock some or all of those credits, then when that entity reports under section 6042 dividends paid to its shareholders, the entity must include distributed tax credits that are treated as dividends.

#### SECTION 5. REQUEST FOR COMMENTS

The Treasury Department and the IRS solicit comments generally on the expected regulations that are described in Section 3 of this notice, other aspects of stripping transactions under section 1286 on which guidance is needed, and the various anticipated information reporting requirements that are described in Section 4 of this notice.

In particular, the Treasury Department and the IRS solicit comments regarding—

- Systems challenges, time needed to implement systems changes to enable affected parties to comply with the anticipated information reporting requirements, and alternative approaches to alleviate systems challenges consistent with the overall objectives for information reporting in this area;
- The application of the principles in this notice to tax credit Build America Bonds under section 54AA and any additional rules that may be necessary to accommodate that application; and
- Whether any particular guidance is needed to limit potential duplicative claims of entitlement to tax credits (e.g., specifying that credits are allowable only to record holders as of a particular time in a particular time zone on a credit allowance date).

Comments should be submitted in writing and can be e-mailed to [notice.comments@irs.counsel.treas.gov](mailto:notice.comments@irs.counsel.treas.gov) (include "Notice 2010-28" in the subject line) or mailed to Office of Associate Chief Counsel (Financial Institutions and Products), Re: Notice 2010-28, CC:FIP:B5, Room 3547, 1111 Constitution Avenue, NW, Washington DC 20224. The due date for the public comments is May 24, 2010. Comments that are submitted will be made available to the public.

## SECTION 6. OMB NUMBER UNDER THE PAPERWORK REDUCTION ACT

The information collection contained in this notice has been approved by the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act (44 U.S.C. chapter 35) under control number 1545–2167. Under the Paperwork Reduction Act, an agency may not conduct or sponsor and a person is not required to respond to a collection of information unless it displays a valid OMB control number.

The collection of information in this notice is in Section 3.03(c). The information is required in order to inform the IRS and holders of qualified tax credit bonds whether the credit coupons relating to those bonds may be stripped. The collections of information are required for the issuer to enjoy the benefit of having these bonds treated as part of a strippable issue. The likely respondents are states or local governments and certain other eligible issuers of qualified tax credit bonds.

We estimate the total number of respondents to be 1,000 and the total annual responses to be 1,000. We estimate it will take 1 hour to comply. Estimates of the annualized cost to respondents for the hour burdens shown are not available at this time.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

## SECTION 7. EFFECTIVE DATE

.01 The effective date of this notice is March 23, 2010.

.02 The interim guidance in Sections 3.02 and 3.03 of this notice applies to—

(1) Stripping transactions (as defined in Section 3.03(b)(3) of this notice) that occur on or after the effective date of this notice; and

(2) Taxable years ending on or after the effective date of this notice for holders of qualified tax credit bonds and of cash or credit coupons stripped from qualified tax credit bonds.

.03 Taxpayers may choose to apply the interim guidance in Section 3.02 of this notice consistently to taxable years ending before the effective date of this notice.

.04 The IRS and the Treasury Department anticipate that the date of applicability of the expected regulations described in this notice will be March 23, 2010. If, and to the extent, the expected regulations differ from the interim guidance in this notice, the different provisions of the final regulations will be applied without adverse retroactive effect.

## SECTION 8. DRAFTING INFORMATION

The principal authors of this notice are Aviva Roth and Timothy Jones of the Office of Associate Chief Counsel (Financial Institutions & Products). For further information regarding this notice, contact Timothy Jones at (202) 622–3980 (not a toll-free call). For questions on earnings and profits, contact Russell P. Subin at (202) 622–7790 (not a toll-free call).

## Life Insurance Reserves — Actuarial Guideline XLIII Notice 2010–29

### SECTION 1. PURPOSE

This notice provides interim guidance to issuers of variable annuity contracts on issues that arise under §§ 807 and 816 of the Internal Revenue Code (Code) as a result of the adoption by the National Association of Insurance Commissioners (NAIC) of Actuarial Guideline XLIII, Commissioners' Annuity Reserve Valuation Methodology (CARVM) for Variable Annuities (AG 43).

### SECTION 2. BACKGROUND

#### *Overview*

.01 A life insurance company is required to account for its obligations to policyholders using reserve methods of accounting. Statutory Accounting Principles (SAP) govern the preparation of the company's annual statement, which is filed with the relevant state insurance regulators. Generally Accepted Accounting Principles (GAAP) govern the preparation

of an insurer's financial statements, which are provided to shareholders, bondholders, banks and rating agencies. GAAP differs in some respects from SAP.

.02 Clear reflection of the income of a life insurance company for federal income tax purposes requires an appropriate measurement of the company's life insurance reserves. Tax accounting rules used to compute the taxable income of a life insurance company differ in some respects from SAP or GAAP, including with respect to the computation of life insurance reserves.

.03 Although all insurance companies are required by the respective states in which they do business to maintain reserves, not all reserves that a company maintains (or is required to maintain) qualify as "life insurance reserves" for Federal income tax purposes.

#### *Use and Computation of Life Insurance Reserves*

.04 Under § 816(a), an insurance company is a life insurance company if the sum of (1) its life insurance reserves, plus (2) unearned premiums, and unpaid losses (whether or not ascertained), on noncancellable life, accident, or health policies not included in life insurance reserves, comprise more than 50 percent of its total reserves.

.05 Section 816(c) defines "total reserves" as the sum of (1) life insurance reserves, (2) unearned premiums, and unpaid losses (whether or not ascertained), not included in life insurance reserves, and (3) all other insurance reserves required by law.

.06 Section 816(b) defines "life insurance reserves" as amounts that are (1) computed or estimated on the basis of recognized mortality or morbidity tables and assumed rates of interest, and (2) set aside to mature or liquidate, either by payment or reinsurance, future unaccrued claims arising from life insurance, annuity, and noncancellable accident and health insurance contracts (including life insurance or annuity contracts combined with noncancellable accident and health insurance) involving, at the time with respect to which the reserve is computed, life, accident, or health contingencies. Reserves generally must be required by law to qualify as life insurance reserves. *See also* § 1.801–4(d) and (e) (setting forth reserves that qualify,