

[1996-36 I.R.B. 32]) was published in the **Federal Register** (60 FR 40796) proposing amendments to the Income Tax Regulations (26 CFR part 1) under section 584 of the Internal Revenue Code. Written comments responding to this notice were received. No public hearing was held because no hearing was requested. After consideration of all comments received, the proposed regulations under section 584 are adopted as revised by this Treasury decision.

Explanation of Provisions

The final regulations modify the diversification test applied to combining, dividing, and resulting common trust funds at the time of a combination or division. Under the existing regulations, which incorporate the diversification test of section 368(a)(2)(F)(ii), Government securities are excluded in determining total assets. These final regulations modify the diversification test so that Government securities are included in determining total assets when applying section 368(a)(2)(F)(ii).

This modified diversification test is the same as that in the final regulations under section 351(e), which deals with transfers to investment companies. These corresponding modifications ensure that a uniform diversification test will be applied to common trust funds and similar investment entities.

The final regulations also update the regulations under section 584 to conform to changes in the law.

Changes to the Proposed Regulations in Response to Comments

I. Clarification that Government securities are not treated as securities of an issuer

Two commentators suggested that the final regulations include specific assurance that Government securities are not treated as securities of an issuer in applying the 25 and 50-percent tests contained in section 368(a)(2)(F)(ii) to mergers and divisions of common trust funds. The proposed regulations provide that Government securities are included in total assets in applying the 25 and 50-percent tests to common trust fund combinations and divisions, but do not specifically state that Government securities are not treated as securities of an issuer. The final

Section 584.—Common Trust Funds

26 CFR 1.584-4: Admission and withdrawal of participants in the common trust fund.

T.D. 8662

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR Part 1

Diversification of Common Trust Funds

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations relating to the diversification of common trust funds at the time of a combination or division. The final regulations affect common trust funds and their participants.

EFFECTIVE DATE: May 2, 1996.

FOR FURTHER INFORMATION CONTACT: Steven Schneider, (202) 622-3060 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

On August 10, 1995, a notice of proposed rulemaking (PS-29-92

regulations clarify that Government securities, while included in total assets, are not treated as securities of an issuer for purposes of the numerator of the 25 and 50-percent tests of section 368(a)(2)(F)(ii).

II. Clarification of the definition of Government securities

One commentator suggested that the regulations broaden the definition of the term *Government securities* to include state and local government obligations. The final regulations do not adopt the suggestion.

Effective Date

These regulations apply to combinations and divisions of common trust funds completed on or after May 2, 1996.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It has also 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, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of this regulation is Brian J. O'Connor, formerly of the Office of Assistant Chief Counsel (Passthroughs and Special Industries). However, other personnel from the IRS and Treasury Department participated in their development.

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Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

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

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

§1.584-2 [Amended]

Par. 2. Section 1.584-2 is amended by:

1. Removing paragraph (b)(1).
2. Removing the paragraph designation (b)(2).

Par. 3. Section 1.584-4 is amended by:

1. Removing paragraphs (a)(1) and (a)(2).
2. Removing the last sentence in paragraph (a) and adding 6 sentences in its place.
3. Adding paragraph (e).

The additions read as follows:

§1.584-4 Admission and withdrawal of participants in the common trust fund.

(a) * * * When a participating interest is transferred by a bank, or by two or more banks that are members of the same affiliated group (within the meaning of section 1504), as a result of the combination of two or more common trust funds or the division of a single common trust fund, the transfer to the surviving or divided fund is not considered to be an admission or a withdrawal if the combining, dividing, and resulting common trust funds have diversified portfolios. For purposes of this paragraph (a), a common trust fund has a diversified portfolio if it satisfies the 25 and 50-percent tests of section 368(a)(2)(F)(ii), applying the relevant provisions of section 368(a)(2)(F). However, Government securities are included in total assets for purposes of the denominator of the 25 and 50-percent tests (unless the Government securities are acquired to meet the 25 and 50-percent tests), but are not treated as securities of an issuer for purposes of the numerator of the 25 and 50-percent tests. In addition, for a transfer of a participating interest in a division of a common trust fund not to be considered an admission or withdrawal, each participant's pro rata interest in each of the resulting common trust funds must be substantially the same as was the participant's pro

rata interest in the dividing fund. However, in the case of the division of a common trust fund maintained by two or more banks that are members of the same affiliated group resulting from the termination of such affiliation, the division will be treated as meeting the requirements of the preceding sentence if the written plans of operation of the resulting common trust funds are substantially identical to the plan of operation of the dividing common trust fund, each of the assets of the dividing common trust fund are distributed substantially pro rata to each of the resulting common trust funds, and each participant's aggregate interest in the assets of the resulting common trust funds of which he or she is a participant is substantially the same as was the participant's pro rata interest in the assets of the dividing common trust fund. The plan of operation of a resulting common trust fund will not be considered to be substantially identical to that of the dividing common trust fund where, for example, the plan of operation of the resulting common trust fund contains restrictions as to the types of participants that may invest in the common trust fund where such restrictions were not present in the plan of operation of the dividing common trust fund.

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(e) *Effective date.* The eighth sentence of paragraph (a) of this section is effective for combinations and divisions of common trust funds completed on or after May 2, 1996.

Margaret Milner Richardson,
Commissioner of Internal Revenue.

Approved March 6, 1996.

Leslie Samuels,
Assistant Secretary of the Treasury.

(Filed by the Office of the Federal Register on May 1, 1996, 8:45 a.m., and published in the issue of the Federal Register for May 2, 1996, 61 F.R. 19546)