

Notice of Proposed Rulemaking and Notice of Public Hearing

Notice of Certain Transfers to Foreign Partnerships and Foreign Corporations

REG-118926-97

AGENCY: Internal Revenue Service (IRS), Treasury.

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

SUMMARY: This document contains proposed regulations under section 6038B of the Internal Revenue Code on information reporting requirements for certain transfers by United States persons to foreign partnerships. The proposed regulations would implement the amendments made by the Taxpayer Relief Act of 1997 that require a United States person who transfers property to a foreign partnership to furnish certain information with respect to such transfers. This document also contains proposed regulations that would amend the information reporting requirements for certain transfers by United States persons to foreign corporations to require the reporting of the transfer of cash. The proposed regulations would provide guidance to United States persons who must furnish this information. This document also provides notice of a public hearing on these proposed regulations.

DATES: Written comments must be received by November 9, 1998. Outlines of topics to be discussed at the public hearing scheduled for November 10, 1998, at 10 a.m., must be received by October 20, 1998.

ADDRESSES: Send submissions to: CC:DOM:CORP:R (REG-118926-97), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered between the hours of 8 a.m. and 5 p.m. to CC:DOM:CORP:R (REG-118926-97), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, DC. Alternatively, taxpayers may submit comments electronically via the Internet by selecting the "Tax Regs" option of the IRS Home Page, or by submitting comments directly

to the IRS Internet site at: http://www.irs.ustreas.gov/prod/tax_reggs/comments.html.

A public hearing has been scheduled to be held in room 2615, Internal Revenue Building, 1111 Constitution Avenue NW, Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning transfers of cash to foreign corporations, Philip L. Tretiak, and concerning transfers to foreign partnerships, Christopher Kelley, 202-622-3860; concerning the hearing and submissions of written comments, Michael Slaughter, 202-622-7190 (not toll-free calls).

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(d)). Comments on the collection of information should be sent to the **Office of Management and Budget**, Attention: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the **Internal Revenue Service**, Attention: IRS Reports Clearance Officer OP:FS:FP, Washington, DC 20224. Comments on the collection of information must be received by November 9, 1998. Comments are specifically requested on:

Whether the proposed collection of information is necessary for the proper performance of the functions of the IRS, including whether the information will have practical utility;

The accuracy of the estimated burden associated with the proposed collection of information (see below);

How the quality, utility, and clarity of the information to be collected may be enhanced;

How the burden of complying with the proposed collection of information may be minimized, including through the application of automated collection techniques or other forms of information technology; and

Estimates of the capital or start-up costs of operation, maintenance, and purchase of services to provide information.

The collection of information in these regulations is in §§1.6038B-1(b) and 1.6038B-2. This information is required by the IRS to identify United States persons who contribute property to foreign partnerships and to ensure the correct reporting of items with respect to those partnerships. The collection of information is mandatory. The likely respondents will be individuals and businesses or other for-profit organizations.

The burden of complying with the proposed collection of information required to be reported on Form 8865 is reflected in the burden for Form 8865.

The burden of complying with the proposed collection of information required to be reported on Form 926 is reflected in the burden for Form 926.

The burden of complying with the proposed collection of information in §1.6038B-2(f)(2) is as follows:

Estimated total annual reporting burden: 250 hours.

Estimated annual burden per respondent: 0.25 hours to 1 hour, with an average of 0.5 hours.

Estimated number of respondents: 500.

Estimated frequency of responses: Once per year.

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 control number assigned by the Office of Management and Budget.

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.

Background

Taxpayer Relief Act of 1997

In the Taxpayer Relief Act of 1997 (TRA 1997), Public Law 105-34 (111 Stat. 983 (1997)), Congress significantly modified the information reporting requirements with respect to foreign partnerships under sections 6038, 6038B and 6046A (and also amended section 6501(c)(8) to provide that the statute of limitations on the assessment of tax under section 6038, 6038B and 6046A does not expire until three years after the information required under those sections is re-

ported). Certain of these modifications also affect reporting requirements with respect to foreign corporations. These regulations under section 6038B are being proposed along with regulations under sections 6038 (reporting with respect to certain foreign partnerships) and 6046A (reporting of certain ownership interests in foreign partnerships). The IRS is also developing a comprehensive form (Form 8865) for reporting under all of these provisions. A draft version of the form will be issued for public comment while the proposed regulations are outstanding.

Section 6038B and Transfers to Foreign Corporations

Section 6038B, as enacted in 1984, provided that United States persons that made certain transfers of property to foreign corporations were required to report those transfers in the manner prescribed by regulations. Prior to the enactment of TRA 1997, section 6038B imposed a penalty for failure to comply with the regulations equal to 25 percent of the gain realized on the exchange, unless the failure was due to reasonable cause and not to willful neglect. Thus, in the case of a transfer of cash or other unappreciated property to a foreign corporation, no penalty was imposed under section 6038B if the transfer was not reported.

Section 1144(c) of TRA 1997 modified the penalty applicable to the failure to furnish information required to be reported under section 6038B. The modified penalty is equal to 10 percent of the fair market value of the property at the time of the transfer.

In response to TRA 1997, Treasury and the IRS issued final regulations under section 6038B (TD 8770 at 63 F.R. 33568; June 19, 1998), in conjunction with regulations under section 367(a), to clarify that transfers to corporations of unappreciated property other than cash that occur on or after July 20, 1998, generally are required to be reported in accordance with §1.6038B-1(b). The preamble to the final regulations stated that rules regarding transfers of cash to foreign corporations would be provided in future regulations.

Section 6038B and Transfers to Foreign Partnerships

Prior to the enactment of TRA 1997, section 1491 imposed an excise tax on

certain transfers of property by United States persons to foreign corporations, partnerships, estates, or trusts. The tax was equal to 35 percent of the fair market value of the property transferred in excess of adjusted basis and any gain recognized on the transfer (built-in gain). Section 1494(c), effective for transfers made after August 20, 1996, imposed a further penalty for a failure to report.

Section 1131(a) of TRA 1997 repealed sections 1491 through 1494. Section 1144 of TRA 1997 amended section 6038B to require a United States person who transfers property to a foreign partnership to report the transfer in the time and manner provided in regulations. The 1997 amendments apply to transfers of property made after August 5, 1997. Notice 98-17 (1998-11 C.B. 6) provided the manner of reporting a transfer under section 6038B made after August 5, 1997, and before January 1, 1998.

Explanation of Provisions

Reporting of Cash Transfers to Foreign Corporations

These proposed regulations provide that transfers of cash to foreign corporations are required to be reported if the U.S. transferor holds, immediately after the transfer, directly or indirectly, a 10-percent interest in the foreign corporation, or the amount of the cash transferred by the transferor or any related person to such foreign corporation or a related foreign corporation during the 12-month period ending on the date of the transfer exceeds \$100,000. The transfer of cash to a foreign corporation will not be required to be reported unless made in a taxable year beginning after the date that final regulations requiring reporting are published in the **Federal Register**.

The IRS and Treasury invite comments on these requirements and the corresponding requirement for foreign partnerships, including a description of the types of transfers which could appropriately be excepted (for example, capital contributions and returns of cash made as part of the normal course of business operations).

Reporting of Transfers to Foreign Partnerships

The proposed regulations would implement the rules of section 6038B by gener-

ally requiring that a United States person that transfers property (including cash) to a foreign partnership in a contribution described in section 721 in exchange for a partnership interest, file a return on Form 8865 "Information Return of U.S. Persons With Respect To Certain Foreign Partnerships", reporting the transfer. Under the statutory exceptions in section 6038B(b)(1), a United States person must report such a contribution only if (1) the United States person holds (immediately after the transfer), directly or indirectly, at least a 10-percent interest in the partnership, or (2) the value of the property transferred (when added to the value of the property transferred by such person to the partnership within the preceding 12 months) exceeds \$100,000 (including the value of property transferred in any transfer not described in section 721, a principal purpose of which is the avoidance of the reporting requirements of these regulations). The proposed regulations would also require a transferor, if still a partner, to notify the IRS when a foreign partnership disposes of appreciated property contributed by the transferor. This information will help in determining whether built-in gain has been properly allocated to and recognized by the U.S. transferor. The proposed regulations provide that certain indirect transferors need not report under this section if certain conditions are met.

A 10-percent interest is defined by cross-reference to section 6046A(d), which in turn cross-references section 6038(e)(3)(C) and regulations issued under that provision. The term means direct or indirect ownership of an interest equal to 10 percent of the capital interest or profits interest in a partnership, and an interest to which 10 percent of the deductions or losses of a partnership are allocated.

Partnerships Excluded From Application of Subchapter K

The reporting requirements of this section shall not apply in respect of any foreign partnership which is an eligible partnership described in §1.761-2(a) that has validly elected pursuant to §1.761-2(b)-(2)(i) to be wholly excluded from the application of subchapter K. Nor shall the reporting requirements of these proposed regulations apply to any foreign partner-

ship validly deemed to have wholly elected out of the provisions of subchapter K as specified in §1.761-2(b)(2)(ii). Taxpayers are reminded, however, that a precondition to being an "electing-out" partnership is that, as provided in §1.761-2(a)(1), "[t]he members of such organization must be able to compute their income without the necessity of computing partnership taxable income." The IRS and Treasury are concerned that in certain cases the necessary books and records are not being maintained to allow verification that such computations can indeed be made without regard to the partnership. If it appears that, in the absence of a reporting requirement under this section, the members of the "electing-out" partnership cannot make such separate computations, this exception to the reporting requirements will be reconsidered.

Reporting of Cash Transfers to Foreign Partnerships

The proposed regulations require the reporting of a cash transfer to a foreign partnership in a contribution otherwise required to be reported under section 6038B and these regulations. Such transfers were required to be reported under Notice 98-17. Reporting of cash transfers will help to ensure that any earnings and appreciation attributable to the cash are reported by the U.S. transferor, and help to prevent United States persons from avoiding the rules applicable to foreign trusts. As noted above with respect to cash contributions to foreign corporations, Treasury and the IRS are interested in receiving comments on specific issues in addition to general comments on this requirement.

Information Required

The proposed regulations would require a United States person to provide certain information with respect to property transferred in a reportable contribution. Appreciated property and intangible property must be listed item by item on the Form 8865. Other items of property may be aggregated and listed according to the following categories: (1) inventory; (2) other tangible trade or business property; (3) cash; (4) securities; and (5) other property.

The proposed regulations provide that a United States person reporting a transfer

to a foreign partnership under section 6038B must identify the other partners in the partnership. This allows the IRS, for example, to determine whether built-in gain is being properly allocated to and recognized by the U.S. transferor under section 704(c). The proposed regulations except from this rule a United States person only required to report because of a transfer of cash, if the transferor holds less than a 10-percent interest in the partnership immediately following the transfer.

Time and Place for Filing

The proposed regulations would require Form 8865 to be filed with the United States person's income tax return (including a partnership return of income) for the year in which the reportable contribution occurs. However, if the transferor is also required to report under proposed regulation §1.6038-3(a), then the transfer must be reported on the Form 8865 (and filed in accordance with §§1.6038-3(e) and (h)) for the foreign partnership's taxable year in which the reportable contribution occurs. Additionally, if required by the instructions to Form 8865, a duplicate Form 8865 must also be filed. The proposed regulations would provide alternative filing deadlines with respect to reportable contributions that occur on or before the date final regulations on this subject are published in the **Federal Register** (see **Effective Dates** portion of this preamble).

Failure to Provide Information

Section 6038B(c)(1) and the proposed regulations provide that a failure by the transferor to properly report a transfer that is required to be reported under section 6038B and these regulations is subject to a penalty equal to 10 percent of the fair market value of the property transferred. This penalty is subject to a \$100,000 limit under section 6038B(c)(3), unless the failure is due to intentional disregard. In addition, the transferor must recognize gain (reduced by gain recognized, with respect to that property, by the transferor after the transfer) as if the property had been sold for its fair market value at the time of the transfer. In addition, section 6501(c)(8) keeps the statute of limitations open with respect to the transferor in the case of a failure to report. Any adjust-

ments to the basis of the partnership or any partner (direct or indirect) as a result of the gain recognized under this provision, shall be made as though the gain was recognized in the year in which the failure to report was finally determined. Section 6038B(c)(2) and the proposed regulations provide a reasonable cause exception to the penalty and gain recognition provisions.

Effective Dates

The amendments to the regulations on the reporting of cash transfers to foreign corporations apply to taxable years beginning after these regulations are published as final regulations in the **Federal Register**.

The proposed regulations on the reporting of transfers to foreign partnerships apply to transfers made on or after January 1, 1998. Notice 98-17 (1998-11 I.R.B. 6) provides reporting requirements for transfers made after August 5, 1997, and before January 1, 1998. The proposed regulations would permit United States persons who made transfers in that period to rely on either Notice 98-17 or the final regulations.

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 has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these proposed regulations. It is hereby certified that the collection of information contained in these proposed regulations will not have a significant economic impact on a substantial number of small entities. This certification is based on the fact that the amount of time required to complete the form and file the information required under these regulations is brief and will not have a significant impact on those small entities that are required to provide notification. Furthermore, the number of small entities that will be required to file the form is not significant. Accordingly, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Internal Revenue

Code, these regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their 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 (preferably a signed original and eight (8) copies) that are submitted timely to the IRS. All comments will be made available for public inspection and copying.

A public hearing has been scheduled for Tuesday, November 10, 1998, at 10 a.m., in room 2615, Internal Revenue Building, 1111 Constitution Avenue NW, Washington, DC. 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 (preferably a signed original and eight (8) copies) by October 20, 1998.

A period of 10 minutes will be allotted for each person 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 proposed regulations are Christopher Kelley and Philip Tretiak of the Office of Associate Chief Counsel (International). 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 is amended by adding an entry in numerical order to read in part as follows:

Authority: 26 U.S.C. 7805 * * *
Section 1.6038B-1 also issued under 26

U.S.C. 6038B.

Section 1.6038B-2 also issued under 26 U.S.C. 6038B. * * *

Par. 2. Section 1.6038B-1 is amended as follows:

1. The section heading is revised.
2. Paragraph (b)(1)(i), first sentence, is revised.
3. The text of paragraph (b)(3) is added.
4. Paragraph (c), first sentence, is revised.
5. Paragraph (g) is revised.

The additions and revisions read as follows:

§1.6038B-1 Reporting of certain transfers to foreign corporations.

* * * * *

(b) *Time and manner of reporting*—(1) *In general*—(i) *Reporting procedure*. Except for stock or securities qualifying under the special reporting rule of paragraph (b)(2) of this section, or cash, which is subject to special rules contained in paragraph (b)(3) of this section, any U.S. person that makes a transfer described in section 6038B(a)(1)(A), 367(d) or (e)(1) is required to report pursuant to section 6038B and the rules of this section and must attach the required information to Form 926 “Return by Transferor of Property to a Foreign Corporation”. * * *

* * * * *

(3) *Special rule for transfers of cash*. A U.S. person that transfers cash must report the transfer of cash to a foreign corporation if—

(i) Such U.S. person holds (immediately after the transfer) directly or indirectly (determined under the rules of sections 318(a) and 6038(e)(2)) at least 10 percent of the total voting power or the total value of the foreign corporation; or

(ii) The amount of cash transferred by such person or any related person (determined under section 267(b)) to such foreign corporation or a related foreign corporation during the 12-month period ending on the date of the transfer exceeds \$100,000.

* * * * *

(c) *Information required with respect to transfers described in section 6038B(a)(1)(A)*. A U.S. person that transfers property to a foreign corporation in

an exchange described in section 6038B(a)(1)(A) (including cash and other unappreciated property) must provide the following information, in paragraphs labeled to correspond with the number or letter set forth in this paragraph (c) and §1.6038B-1T(c)(1) through

(5). * * *

* * * * *

(g) *Effective dates.* This section applies to transfers occurring on or after July 20, 1998, except the first sentence of paragraph (b)(1)(i), paragraph (b)(3), and the first sentence of paragraph (c) apply to taxable years beginning after the date that final regulations are published in the **Federal Register**. See §1.6038B-1T for transfers occurring prior to July 20, 1998.

Par. 6. Section 1.6038B-2 is added to read as follows:

§1.6038B-2 Reporting of certain transfers to foreign partnerships.

(a) *Reporting requirements*—(1) *Requirement to report transfers.* Any United States person that makes a transfer to a foreign partnership in a contribution described in section 721 is required to report pursuant to section 6038B and the rules of this section by filing Form 8865 “Information Return of U.S. Persons With Respect To Certain Foreign Partnerships” attached to the transferor’s income tax return (including a partnership return of income) for the taxable year that includes the date of the transfer by the due date (including extensions) for that return, if—

(i) The United States person holds (immediately after the transfer) directly or indirectly at least a 10-percent interest in the partnership; or

(ii) The value of the property transferred, when added to the value of the property transferred by such person or any related person (described in section 267(b) or 707(b)(1)) to such partnership or a related partnership (described in section 707(b)(1)(B)) during the 12-month period ending on the date of the transfer, exceeds \$100,000. For purposes of determining the relevant amounts, there shall also be taken into account the value of any property transferred in a transfer not subject to section 721, where a principal purpose of such transfer was the avoidance of these reporting requirements.

(2) *Requirement to report dispositions*—(i) *In general.* If a United States

person was required to report a transfer to a foreign partnership under paragraph (b)(1) of property with a fair market value in excess of basis (built-in gain property), and the partnership disposes of the property while such United States person remains a partner, that United States person must report the disposition by filing Form 8865. The form must be attached to, and filed by the due date (including extensions) of, the transferor’s income tax return for the year in which the disposition occurred.

(ii) *Disposition of property in nonrecognition transaction.* If a foreign partnership disposes of contributed built-in gain property in a nonrecognition transaction and substituted basis property is received in exchange, and the substituted basis property has built-in gain under §1.704-3(a)(8), the transferor must report the disposition of the substituted basis property in the same manner as provided for the contributed property.

(3) *Returns to be made*—(i) *Separate returns for each partnership.* If a United States person transfers property to more than one foreign partnership in a taxable year, a separate return must be made by the United States for each partnership.

(ii) *Duplicate form to be filed.* If required by the instructions to Form 8865, a duplicate Form 8865 (including attachments and schedules) must also be filed.

(4) *Time for filing when transferor also required to report under §1.6038-3(a).* If the United States person required to file under this section is also required to file under §1.6038-3(a) for the period in which the transfer occurs, then the United States person must report under this section on the Form 8865 for the foreign partnership’s annual accounting period in which the transfer occurred (not its own taxable year) and file with its income tax return for that year as provided in §§1.6038-3(e) and (h).

(b) *Relief for indirect transferors*—(1) *Requirements.* A United States person otherwise required to file a return under this section with respect to a transfer to a foreign partnership need not file a return if all of the following conditions are met—

(i) The person does not directly own an interest in the foreign partnership;

(ii) The person is required to file a return solely by reason of attribution of ownership from a United States person

(as determined under the rules of section 6038(e)(3) and the regulations thereunder); and

(iii) A United States person from whom the ownership is attributed files all of the information required under section 6038B and this section with respect to the transfer.

(2) *Statement required.* A United States person who does not furnish an information return under the provisions of paragraph (b)(1) of this section must file a statement with the person’s income tax return—

(i) Indicating that the filing requirement has been or will be satisfied;

(ii) Identifying the person who has or will file the return;

(iii) Identifying the IRS Service Center where the return was or will be filed; and

(iv) Providing any additional information as Form 8865 and the accompanying instructions may require.

(c) *Information required with respect to transfers of property.* In respect of transfers described in section 6038B(a)(1)(B), the return must contain information in such form or manner as Form 8865 (and its accompanying instructions) prescribes with respect to reportable events, including—

(1) The name, address, and U.S. taxpayer identification number of the United States person making the transfer;

(2) The name, U.S. taxpayer identification number (if any), and address of the transferee foreign partnership, and the type of entity and country under whose laws the partnership was created or organized;

(3) A general description of the transfer, and of any wider transaction of which it forms a part, including the date of transfer;

(4) The names and addresses of the other partners in the foreign partnership, unless the transfer is solely of cash and the transferor holds less than a 10-percent interest in the transferee foreign partnership immediately after the transfer;

(5) A description of the partnership interest received by the United States person, including a change in partnership interest;

(6) A separate description of each item of contributed property that is appreciated property subject to the allocation rules of section 704(c)(except to the extent that

the property is permitted to be aggregated in making allocations under section 704(c), or is intangible property, including its estimated fair market value and adjusted basis.

(7) A description of other contributed property, not specified in paragraph (c)(6) of this section, aggregated by the following categories (with, in each case, a brief description of the property)—

(i) Stock in trade of the transferor (inventory);

(ii) Tangible property (other than stock in trade) used in a trade or business of the transferor;

(iii) Cash;

(iv) Stock, notes receivable and payable, and other securities; and

(v) Other property.

(d) *Information required with respect to dispositions of property.* In respect of dispositions, the return must contain information in such form or manner as Form 8865 (and its accompanying instructions) prescribes with respect to reportable events, including—

(1) The date and manner of disposition;

(2) The gain and depreciation recapture amounts, if any, realized by the partnership; and

(3) Any such amounts allocated to the United States person.

(e) *Method of reporting.* Except as otherwise provided on Form 8865, or the accompanying instructions, all amounts reported as required under this section must be expressed in United States currency, with a statement of the exchange rates used. All statements required on or with Form 8865 pursuant to this section must be in the English language.

(f) *Reporting under this section not required of partnerships excluded from the application of subchapter K—(1) Election to be wholly excluded.* The reporting requirements of this section will not apply to any United States person in respect of an eligible partnership as described in §1.761-2(a) in which that United States person is a partner, if such partnership has validly elected to be excluded from all of the provisions of subchapter K of chapter 1 of the Internal Revenue Code in the manner specified in §1.761-2(b)(2)(i).

(2) *Deemed excluded.* The reporting requirements of this section will not apply to any United States person in respect of

an eligible partnership as described in §1.761-2(a) in which that United States person is a partner, if such partnership is validly deemed to have elected to be excluded from all of the provisions of subchapter K of chapter 1 of the Internal Revenue Code in accordance with the provisions of §1.761-2(b)(2)(ii).

(g) *Deemed contributions.* If by reason of an adjustment under section 482 or otherwise, a contribution required to be reported under section 6038B(a)(1)(B) and this section is deemed to have been made, the information required to be reported will be furnished timely if filed by the due date (including extensions) of, the taxable year during which the adjustment is made.

(h) *Failure to comply with reporting requirements—(1) Consequences of failure.* If a United States person is required to file a return under paragraph (a) of this section and fails to comply with the reporting requirements of section 6038B and this section, then—

(i) The United States person is subject to a penalty equal to 10 percent of the fair market value of the property at the time of the contribution;

(ii) The United States person will recognize gain (reduced by the amount of any gain recognized, with respect to that property, by the transferor after the transfer) as if the contributed property had been sold for fair market value at the time of the contribution; and

(iii) Adjustments to the basis of the partnership and any relevant partner as a result of gain being recognized under this provision will be made as though the gain was recognized in the year in which the failure to report was finally determined.

(2) *Failure to comply.* A failure to comply with the requirements of section 6038B includes—

(i) The failure to report at the proper time and in the proper manner any information required to be reported under the rules of this section; and

(ii) The provision of false or inaccurate information in purported compliance with the requirements of this section.

(3) *Reasonable cause exception.* Under section 6038B(c)(3) and this section, the provisions of paragraph (h)(1) of this section will not apply if the transferor shows that a failure to comply was due to reasonable cause and not willful neglect. The transferor may attempt to do so by

providing a written statement to the district director having jurisdiction of the taxpayer's return for the year of the transfer, setting forth the reasons for the failure to comply. Whether a failure to comply was due to reasonable cause will be determined by the district director under all facts and circumstances.

(4) *Limitation on penalties.* The penalty under paragraph (h)(1)(i) of this section with respect to any transfer cannot exceed \$100,000, unless the failure to comply with respect to such transfer was due to intentional disregard.

(5) *Statute of limitations.* For exceptions to the limitations on assessment and collection in the event of a failure to provide information under section 6038B, see section 6501(c)(8).

(i) *Definitions—(1) 10-percent interest.* 10-percent interest is defined in sections 6046A(d) and 6038(e)(3)(C) and the regulations thereunder.

(2) *United States person.* United States person is defined in section 7701(a)(30).

(3) *Foreign partnership.* Foreign partnership is defined in section 7701(a)(2) and (5).

(4) *Substituted basis property.* Substituted basis property is defined in section 7701(a)(42).

(5) *Value of the property transferred.* Under section 6038B and this section, the value of the property transferred is the fair market value of the property at the time of its transfer.

(j) *Effective dates—(1) In general.* This section applies to transfers made on or after January 1, 1998. However, for a transfer made prior to the date final regulations are published in the **Federal Register**, Form 8865 will be considered timely filed with respect to a transfer if filed with the taxpayer's income tax return for the first taxable year beginning after the date that final regulations are published in the **Federal Register**.

(2) *Transfers after August 5, 1997 and before January 1, 1998.* A United States person who made a transfer of property required to be reported under section 6038B prior to the effective date of these regulations may satisfy its reporting requirements by reporting in accordance with the provisions of this section.

Michael P. Dolan,
Deputy Commissioner of
Internal Revenue.