tax laws. Therefore, it would be contrary to the public interest to issue this Treasury decision with prior notice under section 553(b) or subject to the effective date limitation of section 553(d) of title 5 of the United States Code.

Pursuant to section 7805(f) of the Internal Revenue Code, these temporary regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

List of Subjects in 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

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

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

Section 1.301–1 also issued under 26 U.S.C. 357(d)(3).

Section 1.301–1T also issued under 26 U.S.C. 357(d)(3). * * *

Par. 2. Section 1.301–1 is amended by adding two new sentences at the end of paragraph (g) to read as follows:

§ 1.301–1 Rules applicable with respect to distributions of money and other property.

* * * * *

(g) * * * This paragraph (g) applies to distributions occurring on or before January 4, 2001. See § 1.301–1T for rules for distributions occurring after January 4, 2001, and for distributions made on or before January 4, 2001 if the distribution is made as part of a transaction described in, or substantially similar to, the transaction in Notice 1999–59, 1999–52 I.R.B. 761, including transactions designed to reduce gain (see § 601.601(d)(2) of this chapter).

* * * * *

Par. 3. Section 1.301–1T is added to read as follows:

§ 1.301–1T Rules applicable with respect to distributions of money and other property (temporary).

(a) through (f). [Reserved] For further guidance, see § 1.301–1(a) through (f).

(g) *Reduction for liabilities*—(1) *General rule.* For the purpose of section 301, no reduction shall be made for the amount of any liability, unless the liability is assumed by the shareholder within the meaning of section 357(d)(1) and (2).

(2) *No reduction below zero.* Any reduction pursuant to paragraph (g)(1) of this section shall not cause the amount of the distribution to be reduced below zero.

(3) *Effective dates*—(i) *In general.* This paragraph (g) applies to distributions occurring after January 4, 2001.

(ii) *Retroactive application.* This paragraph also applies to distributions made on or before January 4, 2001 if the distribution is made as part of a transaction described in, or substantially similar to, the transaction in Notice 1999–59 (1999–52 I.R.B. 761), including transactions designed to reduce gain (see § 601.601(d)(2) of this chapter).

Approved: December 20, 2000.

Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Jonathan Talisman,

Acting Assistant Secretary for Tax Policy.

[FR Doc. 01–200 Filed 1–3–01; 8:45 am]

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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 301

[TD8922]

RIN 1545–AX00

Awards of Attorney's Fees and Other Costs Based Upon Qualified Offers

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to the circumstances under which a party, by reason of having made a qualified offer, will be entitled to an award of reasonable administrative and litigation costs in a civil tax proceeding brought in a court of the United States (including the Tax Court). The regulations implement certain changes made by section 3101(e) of the Internal Revenue Service Restructuring and Reform Act of 1998. They affect taxpayers who make qualified offers. The text of these regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in the Proposed Rules section of this issue of the **Federal Register**.

DATES: *Effective Dates.* These regulations are effective January 3, 2001.

Applicability Date: These regulations apply to qualified offers made in administrative or court proceedings described in section 7430 after January 3, 2001.

FOR FURTHER INFORMATION CONTACT: Thomas D. Moffitt (202) 622–7900 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document contains amendments to the Procedure and Administration Regulations (26 CFR part 301) that reflect changes to section 7430 made by section 3101(e) of the Internal Revenue Service Restructuring and Reform Act of 1998 relating to the circumstances under which taxpayers may recover reasonable administrative and litigation costs in a court proceeding with respect to the determination or refund of any tax, interest or penalty when taxpayers have made a qualified offer.

Explanation of Provisions

In general, a prevailing party may recover the reasonable administrative and litigation costs incurred in administrative and court proceedings if the proceedings relate to the determination or refund of any tax, interest or penalty under the Internal Revenue Code. The regulations provide information concerning the circumstances under which the making of a qualified offer will result in the taxpayer being a prevailing party for purposes of a recovery of costs. In general, a taxpayer is a prevailing party by reason of making a qualified offer if the taxpayer's liability under the last qualified offer would equal or exceed the amount of the taxpayer's liability (determined without regard to interest) attributable to the adjustments included in the last qualified offer that were actually determined by the court through litigation, plus the amount of any additional adjustments included in the last qualified offer that were determined by settlements entered into after the making of the last qualified offer. Adjustments raised by any party subsequent to the making of the last qualified offer are disregarded in determining the liability of the taxpayer to be compared with the liability under the last qualified offer. These regulations apply in multiple taxpayer situations, such as joint returns, but do not set forth any special rules regarding the aggregation or segregation of the qualified offer or liability in situations that may present special circumstances, such as claims for innocent spouse relief. After study, further guidance may be issued elaborating on the treatment of such situations under these regulations.

To qualify as a prevailing party under this rule, in addition to the above,

taxpayers must also satisfy the net worth requirements of section 7430(c)(4)(A)(ii). Furthermore, to qualify for an award, taxpayers must satisfy the remaining requirements of section 7430, such as not unreasonably protracting the proceedings and, for purposes of an award of litigation costs, exhausting their administrative remedies. On the other hand, a taxpayer qualifying as a prevailing party by reason of having made a qualified offer need not substantially prevail on either the amount in controversy or the most significant issue or set of issues presented. Similarly, whether the positions of the United States in the administrative and litigation proceedings were substantially justified is not relevant for an award under the qualified offer rule. An award based upon the taxpayer having made a qualified offer is limited to those reasonable administrative and litigation costs incurred on or after the date of the last qualified offer, with respect to the adjustments that were included in the last qualified offer, and litigated to a judicial determination. If the taxpayer qualifies as a prevailing party without regard to the qualified offer rule, the reasonable administrative and litigation costs to which the taxpayer is thus entitled may not be awarded again by reason of the taxpayer having made a qualified offer.

A qualified offer is a written offer that: (1) Is made by the taxpayer to the United States during the qualified offer period; (2) establishes the taxpayer's liability (determined without regard to interest) by setting forth the amount of the taxpayer's offer on all adjustments at issue in the proceeding at the time the qualified offer is made; (3) is designated as a qualified offer at the time it is made; and (4) remains open at least until the earliest of the date the offer is rejected, the date the trial begins, or the 90th day after the date the offer is made.

The qualified offer period ends on the date which is thirty days before the date the case is first set for trial. In cases that are pending in the United States Tax Court, cases are placed upon a calendar for trial. Each case appearing on a trial calendar is to be called at the time and place scheduled. In determining when the qualified offer period ends for cases in the Tax Court and other courts of the United States using calendars for trial, a case is considered to be set for trial on the date scheduled for the calendar call. Cases may be removed from a trial calendar at any time. Thus, a case may be removed from a calendar before the date that precedes by thirty days the date scheduled for that calendar. To promote the settlement of such cases, the qualified offer period does not end until the case remains on a calendar for trial on the date that precedes by 30 days the scheduled date of the calendar call for that trial session. The qualified offer period may not be extended, although the period during which a qualified offer remains open may extend beyond the end of the qualified offer period.

A taxpayer cannot qualify as a prevailing party by reason of having made a qualified offer if the determination of the court in the proceeding with respect to the adjustments included in the last qualified offer is entered exclusively pursuant to a settlement. Neither can a taxpayer qualify as a prevailing party by reason of having made a qualified offer in any proceeding in which the amount of tax liability is not in issue, including any declaratory judgment proceeding, any proceeding to enforce or quash any summons issued pursuant to the Internal Revenue Code of 1986, and any action to restrain disclosure under section 6110(f).

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 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) does not apply to these regulations and, because these regulations do not impose on small entities a collection of information requirement, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Therefore, a Regulatory Flexibility Analysis is not required. Pursuant to section 7805(f) of the Internal Revenue Code, these temporary regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Drafting Information

The principal author of these regulations is Thomas D. Moffitt, Office of Associate Chief Counsel (Income Tax and Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects in 26 CFR Part 301

Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Penalties, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 301 is amended as follows:

PART 301—PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 continues to read in part as follows:

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

Par. 2. Section 301.7430–7T is added to read as follows:

§ 301.7430–7T Qualified offers (temporary).

(a) *In general.* Section 7430(c)(4)(E) (the qualified offer rule) provides that a party to a court proceeding satisfying the timely filing and net worth requirements of section 7430(c)(4)(A)(ii) shall be treated as the prevailing party if the liability of the taxpayer pursuant to the judgment in the proceeding (determined without regard to interest) is equal to or less than the liability of the taxpayer which would have been so determined if the United States had accepted the last qualified offer of the party as defined in section 7430(g). For purposes of this section, the term *judgment* means the cumulative determinations of the court concerning the adjustments at issue and litigated to a determination in the court proceeding. In making the comparison between the liability under the qualified offer and the liability under the judgment, the taxpayer's liability under the judgment is further modified by the provisions of paragraph (b)(3) of this section. The provisions of the qualified offer rule do not apply if the taxpayer's liability under the judgment, as modified by the provisions of paragraph (b)(3) of this section, is determined exclusively pursuant to a settlement, or to any proceeding in which the amount of tax liability is not in issue, including any declaratory judgment proceeding, any proceeding to enforce or quash any summons issued pursuant to the Internal Revenue Code, and any action to restrain disclosure under section 6110(f). If the qualified offer rule applies to the court proceeding, the determination of whether the liability under the qualified offer would have equaled or exceeded the liability pursuant to the judgment is made by reference to the last qualified offer made with respect to the tax liability at issue in the administrative or court proceeding. An award of reasonable administrative and litigation costs under the qualified offer rule only includes those costs incurred on or after the date

of the last qualified offer and is limited to those costs attributable to the adjustments at issue at the time the last qualified offer was made that were included in the court's judgment other than by reason of settlement. The qualified offer rule is inapplicable to reasonable administrative or litigation costs otherwise awarded to a taxpayer who is a prevailing party under any other provision of section 7430(c)(4). This section sets forth the requirements to be satisfied for a taxpayer to be treated as a prevailing party by reason of the taxpayer making a qualified offer as well as the circumstances leading to the application of the exceptions, special rules, and coordination provisions of the qualified offer rule. Furthermore, this section sets forth the elements necessary for an offer to be treated as a qualified offer under section 7430(g).

(b) *Requirements for treatment as a prevailing party based upon having made a qualified offer.*—(1) *In general.* In order to be treated as a prevailing party by reason of having made a qualified offer, the liability of the taxpayer for the type or types of tax and the taxable year or years at issue in the proceeding, as calculated pursuant to paragraph (b)(2) of this section, based on the last qualified offer, as defined in paragraph (c) of this section, made by the taxpayer in the court or administrative proceeding, must equal or exceed the liability of the taxpayer pursuant to the judgment by the court for the same type or types of tax and the same taxable year or years, as calculated pursuant to paragraph (b)(3) of this section. Furthermore, the taxpayer must meet the timely filing and net worth requirements of section 7430(c)(4)(A)(ii). If all of the adjustments subject to the last qualified offer are settled prior to the entry of the judgment by the court, the taxpayer is not a prevailing party by reason of having made a qualified offer. The taxpayer may, however, still qualify as a prevailing party if the requirements of section 7430(c)(4)(A) are met.

(2) *Liability under the last qualified offer.* For purposes of making the comparison of liability described in paragraph (b)(1) of this section, the taxpayer's liability under the last qualified offer is the change in the taxpayer's liability for the type or types of tax and the taxable year or years at issue in the proceeding from the tax shown on the return or returns (or as previously adjusted) which would have resulted from the acceptance by the United States of the taxpayer's last qualified offer on all of the adjustments at issue in the administrative or court proceeding at the time that offer was made. The portion of a taxpayer's liability that is attributable to adjustments raised by either party after the making of the last qualified offer is not included in the calculation of the liability under that offer. The taxpayer's liability under the last qualified offer is calculated without regard to adjustments to be fully resolved, by stipulation of the parties, through any other pending court or administrative proceeding. Furthermore, the taxpayer's liability under the last qualified offer is calculated without regard to interest unless the taxpayer's liability for, or entitlement to, interest is a contested issue in the administrative or court proceeding and is one of the adjustments included in the last qualified offer.

(3) *Liability pursuant to the judgment.* For purposes of making the comparison of liability described in paragraph (b)(1) of this section, the taxpayer's liability pursuant to the judgment is the change in the taxpayer's liability for the type or types of tax and the taxable year or years at issue in the proceeding from the tax shown on the return or returns (or as previously adjusted), resulting from amounts contained, or to be contained, in the judgment as a result of the court's determinations, and amounts contained in settlements not included in the judgment, that are attributable to all adjustments that were included in the last qualified offer. This liability includes amounts attributable to adjustments included in the last qualified offer and settled by the parties prior to the entry of judgment regardless of whether those amounts are actually included in the judgment entered by the court. The taxpayer's liability pursuant to the judgment does not include amounts attributable to adjustments that are not included in the last qualified offer, even if those amounts are actually included in the judgment entered by the court. The taxpayer's liability pursuant to the judgment is calculated without regard to adjustments to be fully resolved, by stipulation of the parties, through any other pending court or administrative proceeding. Furthermore, the taxpayer's liability pursuant to the judgment is calculated without regard to interest unless the taxpayer's liability for, or entitlement to, interest is a contested issue in the administrative or court proceeding and is one of the adjustments included in the last qualified offer. Where adjustments raised by either party subsequent to the making of the last qualified offer are included in the judgment entered by the court, or are settled prior to the court proceeding, the taxpayer's liability pursuant to the judgment is calculated by treating the subsequently raised adjustments as if they had never been raised.

(c) *Qualified offer*—(1) *In general.* A qualified offer is defined in section 7430(g) to mean a written offer which—

(i) Is made by the taxpayer to the United States during the qualified offer period;

(ii) Specifies the offered amount of the taxpayer's liability (determined without regard to interest, unless interest is a contested issue in the proceeding);

(iii) Is designated at the time it is made as a qualified offer for purposes of section 7430(g); and

(iv) By its terms, remains open during the period beginning on the date it is made and ending on the earliest of the date the offer is rejected, the date the trial begins, or the 90th day after the date the offer is made.

(2) *To the United States.* (i) A qualified offer is made to the United States if it is delivered to the Internal Revenue Service; Office of Appeals; Office of Chief Counsel (including field personnel), Internal Revenue Service; or Department of Justice office or personnel having jurisdiction over the tax matter at issue in the administrative or court proceeding. If those offices or persons are unknown to the taxpayer making the qualified offer, the taxpayer may deliver the offer to the appropriate office, as follows:

(A) If the taxpayer's initial pleading in a court proceeding has been answered, the taxpayer may deliver the offer to the office that filed the answer.

(B) If the taxpayer's petition in the Tax Court has not yet been answered, the taxpayer may deliver the offer to the Office of Chief Counsel, 1111 Constitution Avenue, NW., Washington, DC 20224.

(C) If the taxpayer's initial pleading in a court of the United States other than the Tax Court has not yet been answered, the taxpayer may deliver the offer to the Attorney General of the United States, 950 Pennsylvania Ave., NW., Washington, DC 20530–0001 and for a suit brought in a United States district court, a copy of the offer should also be delivered to the United States Attorney for the district in which the suit was brought.

(D) In any other situation, the taxpayer may deliver the offer to the office that sent the taxpayer the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the Internal Revenue Service Office of Appeals.

(ii) Until an offer is received by the appropriate personnel or office under

this paragraph (c)(2) of this section, it is not considered to have been made, with the following exception. If the offer is deposited in the United States mail, in an envelope or other appropriate wrapper, postage prepaid, properly addressed to the appropriate personnel or office under this paragraph (c)(2), the date of the United States postmark stamped on the cover in which the offer is mailed shall be deemed to be the date of receipt of that offer by the addressee. If any offer is deposited with a designated delivery service, as defined in section 7502(f)(2), in lieu of the United States mail, the provisions of section 7502(f)(1) shall apply in determining whether that offer qualifies for this exception.

(3) *Specifies the offered amount.* A qualified offer specifies the offered amount if it specifies the dollar amount for the liability of the taxpayer, calculated as set forth in paragraph (b)(2) of this section. This amount must be with respect to all of the adjustments at issue in the administrative or court proceeding at the time the offer is made and only those adjustments. The specified amount must be that amount, the acceptance of which by the United States will fully resolve the taxpayer's liability, and only that liability, (determined without regard to adjustments stipulated by the parties to be fully resolved through another pending court or administrative proceeding, or interest, unless interest is a contested issue in the proceeding) for the type or types of tax and the taxable year or years at issue in the proceeding.

(4) *Designated at the time it is made as a qualified offer.* An offer is not a qualified offer unless it is designated in writing at the time it is made that it is a qualified offer for purposes of section 7430(g). An offer made at a time when one or more adjustments not included in the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the Internal Revenue Service Office of Appeals have been raised by the taxpayer and remain unresolved, is not considered to be designated as a qualified offer at the time it is made unless contemporaneously or prior to the making of the qualified offer, the taxpayer has provided the United States with the substantiation and legal and factual arguments necessary to allow for informed consideration of the merits of those adjustments. For example, a taxpayer will be considered to have provided the United States with the necessary substantiation and legal and factual arguments if the taxpayer (or a qualified representative of the taxpayer described in § 601.502 of this chapter) participates in an Appeals office conference, participates in a District Counsel conference, or confers with the Department of Justice and at that time discloses all relevant information regarding the taxpayer's tax matter to the extent such information and its relevance were known or should have been known to the taxpayer at the time of such conference. All relevant information includes, but is not limited to, the legal and factual arguments supporting the taxpayer's position on any adjustments raised by the taxpayer after the issuance of the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the Internal Revenue Service Office of Appeals.

(5) *Remains open.* A qualified offer remains open for acceptance by the Government from the date it is made, as defined in paragraph (c)(2) of this section, at least until the earliest of the date it is rejected in writing by a person with authority to reject the settlement, the date the trial begins, or the 90th day after being received by the United States. The offer, by its written terms, may remain open after the occurrence of one or more of the above-referenced events. Once made, the period during which a qualified offer remains open may be extended by the taxpayer prior to its expiration, but such an extension cannot be used to make an offer meet the minimum period for remaining open required by this paragraph.

(6) *Last qualified offer.* A taxpayer may make multiple qualified offers during the qualified offer period. For purposes of the comparison under paragraph (b) of this section, the making of a qualified offer supersedes any previously made qualified offers. In making the comparison described in paragraph (b) of this section, only the qualified offer made most closely in time to the end of the qualified offer period is compared to the taxpayer's liability under the judgment.

(7) *Qualified offer period.* To constitute a qualified offer, an offer must be made during the qualified offer period. The qualified offer period begins on the date on which the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review in the Internal Revenue Service Office of Appeals is sent to the taxpayer. For this purpose, the date of the notice of claim disallowance will begin the qualified offer period in a refund case. If there has been no notice of claim disallowance in a refund case, the qualified offer period begins on the date on which the answer or other responsive pleading is filed with the court. The qualified offer period ends on the date which is thirty days before the date the case is first set for trial. In determining when the qualified offer period ends for cases in the Tax Court and other courts of the United States using calendars for trial, a case will be considered to be set for trial on the date scheduled for the calendar call. A case may be removed from a trial calendar at any time. Thus, a case may be removed from a calendar before the date that precedes by thirty days the date scheduled for that calendar. The qualified offer period does not end until the case remains on a calendar for trial on the date that precedes by 30 days the scheduled date of the calendar call for that trial session. The qualified offer period may not be extended beyond the periods set forth in this paragraph, although the period during which a qualified offer remains open may extend beyond the end of the qualified offer period.

(d) [Reserved]

(e) *Examples.* The following examples illustrate the provisions of this section:

Example 1. Definition of a judgment. The Internal Revenue Service audits Taxpayer A for year X and issues a notice of proposed deficiency (30-day letter) proposing to disallow deductions 1, 2, 3, and 4. A files a protest and participates in a conference with the Internal Revenue Service Office of Appeals (Appeals). Appeals allows deduction 1, and issues a statutory notice of deficiency for deductions 2, 3, and 4. A's petition to the United States Tax Court for year X never mentions deduction 2. Prior to trial, A concedes deduction 3. After the trial, the Tax Court issues an opinion allowing A to deduct a portion of deduction 4. As used in paragraph (a) of this section, the term *judgment* means the cumulative determinations of the court concerning the adjustments at issue in the court proceeding. Thus, the term judgment does not include deduction 1 because it was never at issue in the court proceeding. Similarly, the term judgment does not include deduction 2 because it was not placed at issue by A in the court proceeding. Although deduction 3 was at issue in the court proceeding, it is not included in the term judgment because it was not determined by the court, but rather by concession or settlement. For purposes of section 7430(c)(4)(e), the term judgment only includes the portion of deduction 4 disallowed by the Tax Court.

Example 2. Liability under the offer and liability under the judgment. Assume the same facts as in *Example 1* except that A makes a qualified offer after the Appeal's conference which is not accepted by the Internal Revenue Service. A's offer is with respect to all adjustments at issue at that time. Those adjustments are deductions 2, 3, and 4. At the conclusion of the litigation, A's entitlement to an award based upon the qualified offer will depend, among other things, on a comparison of the change in A's liability for income tax for year X resulting

from the judgment of the Tax Court with the change that would have resulted had the Internal Revenue Service accepted A's qualified offer. In making this comparison, the term judgment (as discussed in *Example 1*) is modified by including the amounts of settled or conceded adjustments that were at issue at the time the qualified offer was made. Any settled or conceded adjustments that were not at issue at the time the qualified offer was made, either because the settlement or concession occurred before the offer or because the adjustment was not raised until after the offer, are not included in the comparison. Thus, A's offer on deductions 2, 3, and 4 is compared with the change in A's liability resulting from the Tax Court's determination on deduction 4, and the concessions of issues 2 and 3 by A.

Example 3. Offer Must resolve full liability. Assume the same facts as in *Example 2* except that A's offer after the Appeals conference explicitly states that it is only with respect to adjustments 2 and 3 and not with respect to adjustment 4. Even if A's liability pursuant to the judgment, calculated under paragraph (b)(3) of this section as illustrated in *Example 2,* is equal to or less than it would have been had the Internal Revenue Service accepted A's offer after the Appeal's conference, A is not a prevailing party under section 7430(c)(4)(E). This is because a qualified offer must include all adjustments at issue at the time the offer is made. Since A's offer excluded adjustment 4, which was an adjustment at issue at the time the offer was made, it does not constitute a qualified offer pursuant to paragraph (b)(2) of this section.

Example 4. Qualified offer rule inapplicable when all issues settled. Taxpayer B receives a notice of proposed deficiency (30-day letter) proposing to disallow both a personal interest deduction in the amount of $10,000 (Adjustment 1), and a charitable contribution deduction in the amount of $2,000 (Adjustment 2), and to include in income $4,000 of unreported interest income (Adjustment 3). B timely files a protest with Appeals. At the Appeals conference B presents substantiation for the charitable contribution and presents arguments that the interest paid was deductible mortgage interest and that the interest received was held in trust for Taxpayer C. At the conference, B also provides the Appeals officer assigned to B's case a written offer to settle the case for a deficiency of $2,000, exclusive of interest. The offer states that it is a qualified offer for purposes of section 7430(g) and that it will remain open for acceptance by the Internal Revenue Service for a period in excess of 90 days. After considering B's substantiation and arguments, the Appeals Officer accepts the $2,000 offer to settle the case in full. Although B's offer is a qualified offer, because all three adjustments contained in the qualified offer were settled, the qualified offer rule is inapplicable.

Example 5. Qualified offer rule inapplicable when all issues contained in the qualified offer are settled; subsequently raised adjustments ignored. Assume the same facts as in *Example 4* except that B's qualified offer was for a deficiency of $1,800 and the Internal Revenue Service rejected that offer. Subsequently, the Internal Revenue Service issued a statutory notice of deficiency disallowing the three adjustments contained in *Example 4,* and, in addition, disallowing a home office expense in the amount of $5,000 (Adjustment 4). After petitioning the Tax Court, B presents the field attorney assigned to the case with a written offer, which is not designated as a qualified offer for purposes of section 7430(g), to settle the three adjustments that had been the subject of the qualified offer, plus adjustment 4, for a total deficiency of $2,500. After negotiating with B, a settlement is reached on the three adjustments that were the subject of the rejected qualified offer, for a deficiency of $1,800. Adjustment 4 is litigated in the Tax Court and the court determines that B is entitled to the full $5,000 deduction for that adjustment. Consequently, a decision is entered by the Tax Court reflecting the $1,800 settlement amount, which matches exactly the amount of B's only qualified offer in the case. Although the determined liability for adjustments 1, 2, and 3, equal that of the rejected qualified offer, because all three adjustments contained in the qualified offer were settled, the qualified offer rule is inapplicable.

Example 6. Exclusion of adjustments made after the qualified offer is made. Assume the same facts as in *Example 5* except the settlement is reached only on adjustments 1 and 2, for a liability of $1,500. Adjustments 3 and 4 are tried in the Tax Court and in accordance with the court's opinion, the taxpayer has a $300 deficiency attributable to Adjustment 3, and a $1,550 deficiency attributable to adjustment 4. Consequently, a decision is entered reflecting the $1,500 settled amount, the $300 liability on adjustment 3, and the $1,550 liability on adjustment 4. The $3,350 deficiency reflected in the Tax Court's decision exceeds the last (and only) qualified offer made by B. For purposes of determining whether B is a prevailing party as a result of having made a qualified offer in the proceeding, the liability attributable to adjustment 4, which was raised after the last qualified offer was made, is not included in the comparison of B's liability under the judgment with B's offered liability under the last qualified offer. Thus, B's $1,800 liability under the judgment, as modified for purposes of the qualified offer rule comparison, is equal to B's offered liability under the last qualified offer. Because B's liability under the last qualified offer equals or exceeds B's liability under the judgment, as calculated under paragraph (b)(3) of this section, B is a prevailing party for purposes of section 7430. Assuming B satisfies the remaining requirements of section 7430, B may recover those reasonable administrative and litigation costs attributable to adjustment 3. To qualify for any further award of reasonable administrative and litigation costs, B must satisfy the full requirements of section 7430(c)(4)(A).

Example 7. Qualified offer in a refund case. Taxpayer C timely files an amended return claiming a refund of $1,000. This refund claim results from several omitted deductions which, if allowed, would reduce D's tax liability from $10,000 to $9,000. C receives a notice of claim disallowance and files a complaint with the appropriate United States District Court. Subsequently, C makes a qualified offer for a refund of $500. The offer is rejected and after trial the court finds C is entitled to a refund of $700. The change in C's liability from the tax shown on the return that would have resulted from the acceptance of C's qualified offer is a reduction in that liability of $500. The change in C's liability from the tax shown on the return resulting from the judgment of the court is a reduction in that liability of $700. Because C's liability under the qualified offer exceeds C's liability under the judgment, C is a prevailing party for purposes of section 7430. Assuming C satisfies the remaining requirements of section 7430, C may recover those reasonable litigation costs incurred on or after the date of the qualified offer. To qualify for any further award of reasonable administrative and litigation costs C must satisfy the full requirements of section 7430(c)(4)(A).

Example 8. End of qualified offer period when case is removed from tax court trial calendar more than 30 days before scheduled trial calendar. Taxpayer E has petitioned the Tax Court in response to the issuance of a notice of deficiency. E receives notice that the case will be heard on the July trial session in E's city of residence. The scheduled date for the calendar call for that trial session is July 1st. On May 15th, E's motion to remove the case from the July trial session and place it on the October trial session for that city is granted. The scheduled date for the calendar call for the October trial session is October 1st. On May 31st, E delivers a qualified offer to the field attorney assigned to the case. On August 31st, E delivers a revised qualified offer to the field attorney assigned to the case. Neither offer is accepted. The case is tried during the October trial session, and at some time thereafter, a decision is entered by the court. Assume the judgment in the case, as calculated under paragraph (b)(3) of this section, is greater than the amount offered, as calculated under paragraph (b)(2) of this section, in the qualified offer delivered on May 31st, but less than the amount offered, as similarly calculated, in the qualified offer delivered on August 31st. Because the qualified offer period did not end until September 1st, and the offer of August 31st otherwise satisfied the requirements of paragraph (c) of this section, the last qualified offer which is compared to the judgment was the offer delivered on August 31st. Consequently, E is a prevailing party under section 7430(c)(4)(e).

Example 9. End of qualified offer period when case is removed from tax court trial calendar less than 30 days before scheduled trial calendar. Assume the same facts as in *Example 8* except that E's motion was granted on June 15th. Because the qualified offer period had ended on June 1st when the case remained on the July trial session on the date that preceded by 30 days the scheduled

date of the calendar call for that trial session, the offer delivered on May 31st was E's last qualified offer. The August 31st offer is not a qualified offer for purposes of this rule. Consequently, E is not a prevailing party under the qualified offer rule. Therefore, E must satisfy the full requirements of section 7430(c)(4)(A) to qualify for any award of reasonable administrative and litigation costs.

Example 10. When a qualified offer can be made and to whom it must be made. During the examination of Taxpayer F's return, the Internal Revenue Service issues a notice of deficiency without having first issued a 30-day letter. After receiving the notice of deficiency F timely petitions the Tax Court. The next day F mails an offer to the office that issued the notice of deficiency, which offer satisfies the requirements of paragraphs (c)(3), (4), (5) and (6) of this section. This is the only written offer made by F during the administrative or court proceeding, and by its terms it is to remain open for a period in excess of 90 days after the date of mailing to the office issuing the notice of deficiency. The office that issued the notice of deficiency transmitted the offer to the field attorney with jurisdiction over the Tax Court case. After answering the case, the field attorney refers the case to Appeals pursuant to Rev. Proc. 87–24 (1987–1 C.B. 720). After careful consideration, Appeals rejects the offer and holds a conference with F where some adjustments are settled. The remainder of the adjustments are tried in the Tax Court and F's liability resulting from the Tax Court's determinations, when added to F's liability resulting from the settled adjustments, is less than F's liability would have been under the offer rejected by Appeals. Because the Tax Court case had not yet been answered when the offer was sent, F properly mailed the offer to the office that issued the notice of deficiency. Thus, F's offer satisfied the requirements of paragraph (c)(2) of this section. Furthermore, even though F did not receive a 30-day letter, F's offer was made after the beginning of the qualified offer period, satisfying the requirements of paragraph (c)(7) of this section, because the issuance of the statutory notice provided F with notice of the Internal Revenue Service's determination of a deficiency, and the docketing of the case provided F with an opportunity for administrative review in the Internal Revenue Service Office of Appeals under Rev. Proc. 87–24 (1987–1 C.B. 720). Because F's offer satisfied all of the requirements of paragraph (c) of this section, the offer was a qualified offer and F is a prevailing party.

Example 11. Last qualified offer. Assume the same facts as in *Example 10* except that at the Appeals conference F makes a new qualified offer concerning the remaining issues. Because this subsequent qualified offer is closer in time to the end of the qualified offer period than the offer made one day after the petition was filed, the subsequent offer would be the last qualified offer made by F and it is F's liability under this offer which would be compared to F's liability under the judgment to determine whether F was a prevailing party under the qualified offer rule.

Example 12. Substitution of parties permitted under last qualified offer. Taxpayer G receives a 30-day letter and participates in a conference with the Office of Appeals but no agreement is reached. Subsequently, G receives a notice of deficiency and petitions the Tax Court. Upon receiving the Internal Revenue Service's answer to the petition, G sends a qualified offer to the field attorney that signed the answer, by United States mail. The qualified offer stated that it would remain open for more than 90 days. Thirty days after making the offer, G dies and, on motion under Rule 63(a) of the Tax Court's Rules of Practice and Procedure by G's personal representative, H is substituted for G as a party in the Tax Court proceeding. H makes no qualified offers to settle the case and the case proceeds to trial, with the Tax Court issuing an opinion partially in favor of H. Even though H was not a party when the qualified offer was made, that offer constitutes a qualified offer because by its terms, when made, it was to remain open until at least the earlier of the date it is rejected, the date of trial, or 90 days. If the liability of H under that last qualified offer, as determined under paragraph (b)(2) of this section, equals or exceeds the liability under the judgment of the Tax Court, as determined under paragraph (b)(3) of this section, H will be a prevailing party for purposes of an award of reasonable litigation costs under section 7430.

(f) *Effective date.* This section is applicable with respect to qualified offers made in administrative or court proceedings described in section 7430 after January 3, 2001 and before January 5, 2004.

Robert E. Wenzel,

Deputy Commissioner of Internal Revenue.

Approved: December 6, 2000.

Jonathan Talisman,

Acting Assistant Secretary of the Treasury.

[FR Doc. 01–198 Filed 1–3–01; 8:45 am]

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ENVIRONMENTAL PROTECTION AGENCY

40 CFR Part 52

[AZ 004–0033; FRL–6896–8]

Revisions to the Arizona State Implementation Plan, Maricopa County Environmental Services Department

AGENCY: Environmental Protection Agency (EPA).

ACTION: Final rule.

SUMMARY: EPA is finalizing a limited approval and limited disapproval of a revision to the Maricopa County Environmental Services Department (MCESD) portion of the Arizona State Implementation Plan (SIP) concerning particulate matter (PM–10) emissions from open outdoor fires. Under authority of the Clean Air Act as amended in 1990 (CAA or the Act), this action simultaneously approves local rules that regulate these emission sources and directs Arizona State to correct rule deficiencies. EPA is also finalizing a limited approval and a full approval of revisions to the MCESD portion of the Arizona SIP concerning PM–10 emissions from abrasive blasting and non-metallic mineral mining and processing, respectively. The limited approval notifies Arizona State that there are rule deficiencies. These actions were proposed in the **Federal Register** on July 11, 2000.

EFFECTIVE DATE: This rule is effective on February 5, 2001.

ADDRESSES: You can inspect copies of the administrative record for this action at EPA's Region IX office during normal business hours. You can inspect copies of the submitted rule revisions at the following locations:

Environmental Protection Agency, Region IX, 75 Hawthorne Street, San Francisco, CA 94105.

Environmental Protection Agency, Air Docket (6102), Ariel Rios Building, 1200 Pennsylvania Avenue, NW., Washington DC 20460.

Arizona Department of Environmental Quality, 3033 North Central Avenue, Phoenix, AZ 85012.

Maricopa County Environmental Services Department, Air Quality Division, 1001 North Central Avenue, Suite 201, Phoenix, AZ 85004.

FOR FURTHER INFORMATION CONTACT: Al Petersen, Rulemaking Office (AIR–4), Air Division, U.S. Environmental Protection Agency, Region IX, 75 Hawthorne Street, San Francisco, CA 94105, Telephone: (415) 744–1135.

SUPPLEMENTARY INFORMATION: Throughout this document, ''we,'' ''us'' and ''our'' refer to EPA.

I. Proposed Action

On July 11, 2000 (65 FR 42649), EPA proposed a limited approval and limited disapproval of the following rule that was submitted for incorporation into the Arizona SIP.