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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

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Arbitrage and Private Activity Restrictions Applicable to Tax-exempt Bonds Issued by State and Local Governments; Investment-type Property (prepayment); Private Loan (prepayment).

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations on the arbitrage and private activity restrictions applicable to tax-exempt bonds issued by State and local governments. These regulations affect issuers of tax-exempt bonds and provide guidance on the definitions of investment-type property and private loan to help issuers comply with the arbitrage and private activity restrictions.

DATES: Effective Date: These regulations are effective October 3, 2003.

Applicability Date: For dates of applicability, see §§1.141-15(b)(3) and 1.148-11(j) of these regulations.

FOR FURTHER INFORMATION CONTACT: Johanna Som de Cerff (202) 622-3980 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

**Background**

This document amends the Income Tax Regulations (26 CFR part 1) under sections 141 and 148 of the Internal Revenue Code by providing rules for determining whether a prepayment for property or services results in a private loan or investment-type property (the final regulations). On April 17, 2002, the IRS published in the **Federal Register** a notice of proposed rulemaking (REG-113526-98; REG-105369-00)(67 FR 18835)(the proposed regulations). The proposed regulations modify §§1.141-5(c)(2) and 1.148-1(e) of the Income Tax Regulations to establish which prepayments for property or services give rise to a private loan under section 141(c) or investment-type property under section 148(b)(2)(D). On September 25, 2002, the IRS held a public hearing on the proposed regulations. Written comments responding to the proposed regulations were also received. After consideration of all the comments, the proposed regulations are adopted as amended by this Treasury decision. The revisions are discussed below.

**Explanation of Provisions**

I. Investment-type Property

A. Existing regulations

The existing regulations, at §1.148-1(e)(2), contain rules for determining when a prepayment for property or services results in

investment-type property. Under that provision, a prepayment generally gives rise to investment-type property if a principal purpose for prepaying is to receive an investment return from the time the prepayment is made until the time payment otherwise would be made. However, a prepayment does not give rise to investment-type property under the existing regulations if (1) it is made for a substantial business purpose other than investment return and the issuer has no commercially reasonable alternative to the prepayment (the business purpose exception); or (2) prepayments on substantially the same terms are made by a substantial percentage of persons who are similarly situated to the issuer but who are not beneficiaries of tax-exempt financing (the customary exception).

B. Business purpose exception

The proposed regulations narrow the scope of the business purpose exception. Under the proposed regulations, a prepayment meets the business purpose exception only if the primary purpose for the prepayment is to accomplish one or more substantial business purposes that (1) are unrelated to any investment return based on the time value of money and (2) cannot be accomplished without the prepayment.

Commentators suggested that the business purpose exception in the proposed regulations would have limited usefulness and that the language in the existing regulations is superior. However, as

discussed in the preamble to the proposed regulations, the business purpose exception in the existing regulations was intended to be a narrow exception and has raised difficult interpretive questions. For example, in many instances it may be unclear whether the alternatives available to the issuer are "commercially reasonable." The IRS and Treasury Department have considered all of the comments relating to the business purpose exception and have concluded that a standard that considers whether one or more business purposes and/or commercially reasonable alternatives exist is not an administrable test for determining whether prepayments give rise to investment-type property. Therefore, based on tax administration considerations and the broad scope of the investment-type property concept, the final regulations delete the business purpose exception. However, the final regulations provide that the Commissioner may, by published guidance, set forth additional circumstances in which a prepayment does not give rise to investment-type property.

C. Customary exception

The proposed regulations retain the customary exception in its present form. Commentators expressed concern that the customary exception may be difficult to apply in some cases. They suggested that the regulations identify examples of prepayments that satisfy the exception. The final regulations retain the customary exception and indicate that it generally applies based on all the facts and

circumstances. In addition, the final regulations contain a safe harbor under which a prepayment is deemed to satisfy the customary exception if: (1) the prepayment is made for maintenance, repair, or an extended warranty with respect to personal property (for example, automobiles or electronic equipment), or updates or maintenance or support services with respect to computer software; and (2) the same maintenance, repair, extended warranty, updates or maintenance or support services, as applicable, are regularly provided to nongovernmental persons on the same terms.

D. Certain prepayments to acquire a supply of natural gas or electricity

1. Prepayments for Natural Gas

The proposed regulations add an exception to the definition of investment-type property for certain natural gas prepayments that are made by or for one or more utilities that are owned by a governmental person, as defined in §1.141-1(b) (for example, if a joint action agency acquires a natural gas supply for one or more municipal gas or electric utilities). The exception applies only if at least 95 percent of the natural gas purchased with the prepayment is to be consumed by retail customers in the service area of a municipal gas utility, or used to produce electricity that will be furnished to retail customers that a municipal electric utility is obligated to serve under state or Federal law (the use requirement). For this purpose, the service area of a municipal gas utility is defined as

(1) any area throughout which the municipal utility provided (at all times during the five-year period ending on the issue date) gas transmission or distribution service, and any area that is contiguous to such an area, or (2) any area where the municipal utility is obligated under state or Federal law to provide gas distribution services as provided in such law.

Some commentators recommended that the 95 percent threshold be reduced to 85 percent. These commentators stated that various factors make it difficult for municipal gas utilities to determine in advance the precise quantity of gas supplies they will need to serve their customers during a given period. These factors include a limited capability to store gas and variations in demand due to circumstances beyond the utilities' control, such as economic conditions and the weather. In recognition of these unique factors, the final regulations reduce the 95 percent threshold to 90 percent.

Some commentators recommended that the use requirement apply based on the issuer's reasonable expectations as of the issue date. To ensure that the prepaid gas is consumed by retail customers in the service area of the municipal utility, the final regulations retain the requirement that the prepaid gas supply actually be used for a qualifying purpose.

Some commentators suggested that the use of natural gas to fuel the transportation of the prepaid gas supply on a pipeline should be

a qualifying use under the natural gas exception. The final regulations adopt this comment. Under the final regulations, the use of gas to fuel the pipeline transportation of the prepaid gas supply is a qualifying use and is not pro-rated based on the amount of qualified and nonqualified use of the remaining prepaid gas.

Commentators indicated that most municipal gas and electric utilities do not have an obligation to serve that arises under state or Federal law. These commentators suggested replacing the "obligation to serve" requirement for municipal electric utilities with a service area rule that is similar to the rule for municipal gas utilities. The final regulations adopt this comment.

Commentators also recommended that the definition of service area be expanded to include any area recognized as the service area of the municipal utility under state or Federal law. The final regulations adopt this comment.

Commentators requested clarification that sales to governmental persons are qualifying sales under the use test. Commentators also requested clarification that a retail customer of a municipal utility is a qualifying end-user even if the prepayment was made by or for another municipal utility. The final regulations do not provide that all sales to governmental persons, or to retail customers of a municipal utility, are qualifying sales. Rather, the final regulations clarify that, in the case of a natural gas prepayment by

or for one or more municipal utilities (each, the issuing municipal utility), the use of prepaid gas is a qualifying use if the gas is: (1) furnished to retail gas customers of the issuing municipal utility who are located in the natural gas service area of the issuing municipal utility (other than sales of gas to produce electricity for sale); (2) used by the issuing municipal utility to produce electricity that will be furnished to retail electric customers of the issuing municipal utility who are located in the electricity service area of the issuing municipal utility; (3) used by the issuing municipal utility to produce electricity that will be sold to a municipal utility and furnished to retail electric customers of the purchaser who are located in the electricity service area of the purchaser; (4) sold to a municipal utility if the requirements of (1), (2) or (3) of this paragraph are satisfied by the purchaser (treating the purchaser as the issuing municipal utility); or (5) used to fuel the transportation of the prepaid gas supply on a pipeline. Thus, for example, the sale of gas or electricity by the issuing municipal utility directly to customers of another municipal utility is not a qualifying use.

Some commentators recommended that the final regulations define "retail customer" as a customer that is not purchasing for resale. The final regulations provide that a retail customer is a customer that purchases natural gas or electricity, as applicable, other than



for resale. The final regulations also clarify that the consumption of natural gas by a nongovernmental person to produce electricity for sale is not a qualifying use of natural gas under the 90 percent use test.

Some commentators requested clarification of which "contiguous" areas may be treated as part of a municipal utility's service area. One commentator suggested that contiguous areas should not be considered part of the service area. To provide clarity, and in light of the expansion of the service area definition to include any area recognized as the service area under state or Federal law, the final regulations eliminate contiguous areas from the definition of service area.

Some commentators suggested that the definition of service area should be expanded to include any area "in which" (rather than "throughout which") the municipal utility provided service during the five-year period. To ensure that the gas or electricity is consumed by customers in an area recognized as the service area of a municipal utility under state or Federal law, or throughout which the municipal utility provided service during the five-year period, the final regulations do not adopt this comment.

## 2. Prepayments for Electricity

Some commentators suggested that the natural gas exception should be expanded to include prepayments for electricity. These

commentators stated that the restructuring of the electric power industry has affected municipal electric utilities in a manner that is similar to the effect that deregulation of the natural gas industry had on municipal gas utilities. These commentators stated that restructuring has threatened the ability of municipal electric utilities to obtain a secure supply of electric power on commercially reasonable terms, and that electric power prepayment transactions are necessary to obtain a guaranteed supply of electric power on favorable terms in light of restructuring.

The final regulations add an exception to the definition of investment-type property for certain electricity prepayments that are made by or for one or more municipal utilities (for example, if a joint action agency acquires electricity for one or more municipal electric utilities). The exception applies only if at least 90 percent of the prepaid electricity financed by the issue is used for a qualifying use. For this purpose, electricity is used for a qualifying use if it is to be: (1) furnished to retail electric customers of the issuing municipal utility who are located in the electricity service area of the issuing municipal utility; or (2) sold to a municipal utility and furnished to retail electric customers of the purchaser who are located in the electricity service area of the purchaser.

### 3. Remedial Actions

The preamble to the proposed regulations states that issuers may apply principles similar to the rules of §1.141-12 to cure a violation of the use requirement. Commentators requested clarification regarding which remedies under §1.141-12 are available for this purpose. The final regulations provide that issuers may apply principles similar to the rules of §1.141-12 to cure a violation of the 90 percent use requirement, and that the "redemption or defeasance" remedy in §1.141-12(d) and the "alternative use of disposition proceeds" remedy in §1.141-12(e) are available for this purpose.

Some commentators requested clarification of the amount of nonqualified bonds that must be redeemed or defeased under the "redemption or defeasance" remedy. Under the final regulations, the amount of nonqualified bonds is determined in the same manner as for output contracts taken into account under the private business tests, including the principles of §1.141-7(d), treating nonqualified sales of gas or electricity as satisfying the benefits and burdens test under §1.141-7(c)(1). Commentators also suggested that the definition of "nonqualified bonds" under §1.141-12 may require excessive amounts of bonds to be retired. The IRS and Treasury Department are considering this comment in connection with possible amendments to §1.141-12.

#### 4. Commodity Swap Contracts

The proposed regulations provide that a transaction will not fail to qualify for the natural gas exception by reason of any commodity swap contract that may be entered into between the issuer and an unrelated party (other than the gas supplier), or between the gas supplier and an unrelated party (other than the issuer), so long as each swap contract is an independent contract. For this purpose, the proposed regulations provide that a swap contract is an independent contract if the obligation of each party to perform under the swap contract is not dependent on performance by any person (other than the other party to the swap contract) under another contract (for example, a gas supply contract or another swap contract). Notice 2002-52 (2002-30 I.R.B. 187), provides that a natural gas commodity swap contract will not fail to be an independent contract solely because the swap contract may terminate in the event of a failure of a gas supplier to deliver gas for which the swap contract is a hedge.

Commentators generally agreed with the provision on swap contracts in the proposed regulations, as modified by Notice 2002-52. The final regulations retain the provision on commodity swap contracts for natural gas prepayments, as modified by Notice 2002-52, and expand it to apply to electricity prepayments.

E. De minimis prepayments

The proposed regulations add an exception for prepayments made within 90 days of the date of delivery of all the property or services to which the prepayment relates. Commentators recommended that the exception apply based on reasonable expectations. The final regulations adopt this comment. This change to a reasonable expectations standard is intended to permit a prepayment to qualify for the de minimis exception even if an unexpected event beyond the control of the issuer causes delivery of the property or services to be delayed beyond the 90-day period. The reasonable expectations standard does not, however, apply to any change to the terms of the prepayment other than an unexpected delay in delivery.

## II. Private Loans

The existing regulations, at §1.141-5(c)(2)(ii), provide rules for determining whether a prepayment for property or services is treated as a loan for purposes of the private loan financing test. The existing regulations for private loans are similar to the existing regulations in §1.148-1(e)(2) for determining whether a prepayment gives rise to investment-type property, except that the private loan regulations focus on whether the prepayment provides a benefit of tax-exempt financing to the seller. The final regulations amend the private loan provisions of §1.141-5(c)(2) to conform to the amendments to the definition of investment-type property in the final regulations.

### III. Tables of Contents

The final regulations amend the tables of contents in §§1.141-0 and 1.148-0 to reflect the final regulations and certain previously issued regulations under sections 141 and 148.

#### **Effective Dates**

The final regulations apply to bonds sold on or after October 3, 2003. In addition, issuers may apply the final regulations to bonds sold before October 3, 2003, that are subject to §§1.141-5 and 1.148-1.

#### **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 has also 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 the rule does not impose a collection of information on small entities, the provisions of the Regulatory Flexibility Act (5 U.S.C. 601 et seq.) do not apply.

#### **Drafting Information**

The principal authors of these regulations are Rebecca L. Harrigal and Johanna Som de Cerff, Office of Chief Counsel (TE/GE), IRS, and Stephen J. Watson, Office of Tax Policy, Treasury

Department. However, other personnel from the IRS and Treasury Department participated in their development.

**List of Subjects in 26 CFR Part 1**

Income taxes, Reporting and recordkeeping requirements.

**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 \* \* \*

Par. 2. Section 1.141-0 is amended by revising the entry for §1.141-15(b) to read as follows:

§1.141-0 Table of contents.

\* \* \* \* \*

§1.141-15 Effective dates.

\* \* \* \* \*

- (b) Effective dates.
- (1) In general.
- (2) Certain short-term arrangements.
- (3) Certain prepayments.

\* \* \* \* \*

Par. 3. In §1.141-5, paragraph (c)(2)(ii) is revised and paragraphs (c)(2)(iii) and (c)(2)(iv) are added to read as follows:

§1.141-5 Private loan financing test.

\* \* \* \* \*

(c) \* \* \*

(2) \* \* \*

(ii) Certain prepayments treated as loans. Except as otherwise provided, a prepayment for property or services, including a prepayment for property or services that is made after the date that the contract to buy the property or services is entered into, is treated as a loan for purposes of the private loan financing test if a principal purpose for prepaying is to provide a benefit of tax-exempt financing to the seller. A prepayment is not treated as a loan for purposes of the private loan financing test if--

(A) Prepayments on substantially the same terms are made by a substantial percentage of persons who are similarly situated to the issuer but who are not beneficiaries of tax-exempt financing;

(B) The prepayment is made within 90 days of the reasonably expected date of delivery to the issuer of all of the property or services for which the prepayment is made; or

(C) The prepayment meets the requirements of §1.148-1(e)(2)(iii)(A) or (B) (relating to certain prepayments to acquire a supply of natural gas or electricity).

(iii) Customary prepayments. The determination of whether a prepayment satisfies paragraph (c)(2)(ii)(A) of this section is generally made based on all the facts and circumstances. In



addition, a prepayment is deemed to satisfy paragraph (c)(2)(ii)(A) of this section if--

(A) The prepayment is made for--

(1) Maintenance, repair, or an extended warranty with respect to personal property (for example, automobiles or electronic equipment); or

(2) Updates or maintenance or support services with respect to computer software; and

(B) The same maintenance, repair, extended warranty, updates or maintenance or support services, as applicable, are regularly provided to nongovernmental persons on the same terms.

(iv) Additional prepayments as permitted by the Commissioner. The Commissioner may, by published guidance, set forth additional circumstances in which a prepayment is not treated as a loan for purposes of the private loan financing test.

\* \* \* \* \*

Par. 4. Section 1.141-15 is amended by adding paragraph (b)(3) to read as follows:

§1.141-15 Effective dates.

\* \* \* \* \*

(b) \* \* \*

(3) Certain prepayments. Except as provided in paragraph (c) of this section, paragraphs (c)(2)(ii), (c)(2)(iii) and (c)(2)(iv) of

§1.141-5 apply to bonds sold on or after October 3, 2003. Issuers may apply paragraphs (c)(2)(ii), (c)(2)(iii) and (c)(2)(iv) of §1.141-5, in whole but not in part, to bonds sold before October 3, 2003, that are subject to §1.141-5.

Par. 5. Section 1.148-0 is amended by:

1. Adding entries in paragraph (c) for §1.148-1, paragraphs (e)(1) through (e)(3).

2. Adding entries in paragraph (c) for §1.148-11, paragraphs (b)(4), (h), (i) and (j).

The additions read as follows:

§1.148-0 Scope and table of contents.

\* \* \* \* \*

(c) Table of contents.

\* \* \* \* \*

§1.148-1 Definitions and elections.

\* \* \* \* \*

(e) \* \* \*

- (1) In general.
- (2) Prepayments.
- (3) Certain hedges.

\* \* \* \* \*

§1.148-11 Effective dates.

(b) \* \* \*

(4) No elective retroactive application for safe harbor for establishing fair market value for guaranteed investment contracts and investments purchased for a yield restricted defeasance escrow.  
\* \* \* \* \*

(h) Safe harbor for establishing fair market value for guaranteed investment contracts and investments purchased for a yield restricted defeasance escrow.

(i) Special rule for investments purchased for a yield restricted defeasance escrow.

(j) Certain prepayments.

Par. 6. In §1.148-1, paragraphs (e)(1) and (2) are revised to read as follows:

§1.148-1 Definitions and elections.

\* \* \* \* \*

(e) Investment-type property--(1) In general. Investment-type property includes any property, other than property described in section 148(b)(2)(A), (B), (C) or (E), that is held principally as a passive vehicle for the production of income. For this purpose, production of income includes any benefit based on the time value of money.

(2) Prepayments--(i) In general--(A) Generally. Except as otherwise provided in this paragraph (e)(2), a prepayment for property or services, including a prepayment for property or services that is made after the date that the contract to buy the property or services is entered into, also gives rise to investment-type property if a principal purpose for prepaying is to receive an investment return from the time the prepayment is made until the time payment

otherwise would be made. A prepayment does not give rise to investment-type property if--

(1) Prepayments on substantially the same terms are made by a substantial percentage of persons who are similarly situated to the issuer but who are not beneficiaries of tax-exempt financing;

(2) The prepayment is made within 90 days of the reasonably expected date of delivery to the issuer of all of the property or services for which the prepayment is made; or

(3) The prepayment meets the requirements of paragraph (e)(2)(iii)(A) or (B) of this section.

(B) Example. The following example illustrates an application of this paragraph (e)(2)(i):

Example. Prepayment after contract is executed. In 1998, City A enters into a ten-year contract with Company Y. Under the contract, Company Y is to provide services to City A over the term of the contract and in return City A will pay Company Y for its services as they are provided. In 2004, City A issues bonds to finance a lump sum payment to Company Y in satisfaction of City A's obligation to pay for Company Y's services to be provided over the remaining term of the contract. The use of bond proceeds to make the lump sum payment constitutes a prepayment for services under paragraph (e)(2)(i) of this section, even though the payment is made after the date that the contract is executed.

(ii) Customary prepayments. The determination of whether a prepayment satisfies paragraph (e)(2)(i)(A)(1) of this section is generally made based on all the facts and circumstances. In

addition, a prepayment is deemed to satisfy paragraph (e)(2)(i)(A)(1) of this section if--

(A) The prepayment is made for--

(1) Maintenance, repair, or an extended warranty with respect to personal property (for example, automobiles or electronic equipment); or

(2) Updates or maintenance or support services with respect to computer software; and

(B) The same maintenance, repair, extended warranty, updates or maintenance or support services, as applicable, are regularly provided to nongovernmental persons on the same terms.

(iii) Certain prepayments to acquire a supply of natural gas or electricity--(A) Natural gas prepayments. A prepayment meets the requirements of this paragraph (e)(2)(iii)(A) if--

(1) It is made by or for one or more utilities that are owned by a governmental person, as defined in §1.141-1(b) (each of which is referred to in this paragraph (e)(2)(iii)(A) as the issuing municipal utility), to purchase a supply of natural gas; and

(2) At least 90 percent of the prepaid natural gas financed by the issue is used for a qualifying use. Natural gas is used for a qualifying use if it is to be--

(i) Furnished to retail gas customers of the issuing municipal utility who are located in the natural gas service area of the

issuing municipal utility, provided, however, that gas used to produce electricity for sale shall not be included under this paragraph (e)(2)(iii)(A)(2)(i);

(ii) Used by the issuing municipal utility to produce electricity that will be furnished to retail electric customers of the issuing municipal utility who are located in the electricity service area of the issuing municipal utility;

(iii) Used by the issuing municipal utility to produce electricity that will be sold to a utility that is owned by a governmental person and furnished to retail electric customers of the purchaser who are located in the electricity service area of the purchaser;

(iv) Sold to a utility that is owned by a governmental person if the requirements of paragraph (e)(2)(iii)(A)(2)(i), (ii) or (iii) of this section are satisfied by the purchaser (treating the purchaser as the issuing municipal utility); or

(v) Used to fuel the pipeline transportation of the prepaid gas supply acquired in accordance with this paragraph (e)(2)(iii)(A).

(B) Electricity prepayments. A prepayment meets the requirements of this paragraph (e)(2)(iii)(B) if--

(1) It is made by or for one or more utilities that are owned by a governmental person (each of which is referred to in this

paragraph (e)(2)(iii)(B) as the issuing municipal utility) to purchase a supply of electricity; and

(2) At least 90 percent of the prepaid electricity financed by the issue is used for a qualifying use. Electricity is used for a qualifying use if it is to be--

(i) Furnished to retail electric customers of the issuing municipal utility who are located in the electricity service area of the issuing municipal utility; or

(ii) Sold to a utility that is owned by a governmental person and furnished to retail electric customers of the purchaser who are located in the electricity service area of the purchaser.

(C) Service area. For purposes of this paragraph (e)(2)(iii), the service area of a utility owned by a governmental person consists of--

(1) Any area throughout which the utility provided, at all times during the 5-year period ending on the issue date--

(i) In the case of a natural gas utility, natural gas transmission or distribution service; and

(ii) In the case of an electric utility, electricity distribution service; and

(2) Any area recognized as the service area of the utility under state or Federal law.

(D) Retail customer. For purposes of this paragraph (e)(2)(iii), a retail customer is a customer that purchases natural gas or electricity, as applicable, other than for resale.

(E) Commodity swaps. A prepayment does not fail to meet the requirements of this paragraph (e)(2)(iii) by reason of any commodity swap contract that may be entered into between the issuer and an unrelated party (other than the gas or electricity supplier), or between the gas or electricity supplier and an unrelated party (other than the issuer), so long as each swap contract is an independent contract. A swap contract is an independent contract if the obligation of each party to perform under the swap contract is not dependent on performance by any person (other than the other party to the swap contract) under another contract (for example, a gas or electricity supply contract or another swap contract); provided, however, that a commodity swap contract will not fail to be an independent contract solely because the swap contract may terminate in the event of a failure of a gas or electricity supplier to deliver gas or electricity for which the swap contract is a hedge.

(F) Remedial action. Issuers may apply principles similar to the rules of §1.141-12, including §1.141-12(d) (relating to redemption or defeasance of nonqualified bonds) and §1.141-12(e) (relating to alternative use of disposition proceeds), to cure a violation of paragraph (e)(2)(iii)(A)(2) or (e)(2)(iii)(B)(2) of this



section. For this purpose, the amount of nonqualified bonds is determined in the same manner as for output contracts taken into account under the private business tests, including the principles of §1.141-7(d), treating nonqualified sales of gas or electricity under this paragraph (e)(2)(iii) as satisfying the benefits and burdens test under §1.141-7(c)(1).

(iv) Additional prepayments as permitted by the Commissioner.

The Commissioner may, by published guidance, set forth additional circumstances in which a prepayment does not give rise to investment-type property.

\* \* \* \* \*

Par. 7. Section 1.148-11 is amended by adding paragraph (j) to read as follows:

§1.148-11 Effective dates.

\* \* \* \* \*

(j) Certain prepayments. Section 1.148-1(e)(1) and (2) apply to bonds sold on or after October 3, 2003. Issuers may apply §1.148-1(e)(1) and (2), in whole but not in part, to bonds sold before October 3, 2003, that are subject to §1.148-1.

Dale F. Hart,

Acting Deputy Commissioner for Services and Enforcement.

Approved: July 25, 2003.

Pamela F. Olson,

Assistant Secretary of the Treasury.