

that the taxpayer elects to treat the sale of securities as a sale of qualified securities under section 1042(a) and must contain the following information: (1) A description of the qualified securities sold, including the type and number of shares; (2) The date of the sale of the qualified securities; (3) The adjusted basis of the qualified securities; (4) The amount realized upon the sale of the qualified securities; (5) The identity of the ESOP or eligible worker-owned cooperative to which the qualified securities were sold; and (6) If the sale was part of a single interrelated transaction under a prearranged agreement between taxpayers involving other sales of qualified securities, the names and taxpayer identification numbers of the other taxpayers under the agreement and the number of shares sold by the other taxpayers.

Section 1.1042-1T, A-3(b) further provides that, if the taxpayer has purchased qualified replacement property at the time of the election, the taxpayer must attach as part of the statement of election a *statement of purchase* describing the qualified replacement property, the date of the purchase, and the cost of the property, and declaring such property to be qualified replacement property with respect to the sale of qualified securities.

The statement of purchase must be notarized no later than 30 days after the purchase. The purpose of the statement of purchase is to identify qualified replacement property with respect to a sale of qualified securities. The qualified replacement property will have its cost basis reduced under section 1042(d) to reflect the gain on the sale of qualified securities that is being deferred by the taxpayer. Upon subsequent disposition of the qualified replacement property by the taxpayer, the deferred gain will be recognized by the taxpayer under section 1042(e). Under section 1042(f), the filing of the statement of purchase of qualified replacement property (or a statement of the taxpayer's intention not to purchase replacement property) will begin the statutory period for assessment of any deficiency with respect to gain arising from the sale of the qualified securities. The purpose of the 30-day notarization requirement is to provide a contemporaneous identification of replacement property.

However, the 30-day notarization requirement leads to frequent mistakes by taxpayers and their advisors. Taxpayers are often unaware of this requirement and become aware of it only when they prepare their tax returns for the year of sale to the ESOP. By this

time, the 30-day period is typically past because purchases of replacement property may have been made up to one year before. A number of private letter rulings have been issued granting relief to taxpayers in these situations as long as the statements were notarized shortly after the taxpayer became aware of the requirement and it was represented that the property listed was the only replacement property purchased for this sale.

A number of commentators on the temporary and proposed regulations criticized this requirement as without statutory authority, a trap for the unwary, and inconsistent with the definition of the qualified replacement period in section 1042(c)(3).

#### *Proposed Amendment to the Regulations*

In order to facilitate taxpayer compliance with the temporary regulations concerning identification of qualified replacement property through notarization of the statements of purchase, the proposed amendment to the temporary regulations would modify § 1.1042-1T, A-3(b) to provide that the notarization requirements for the *statement of purchase* are satisfied if the taxpayer's statement of purchase is notarized not later than the time the taxpayer files the income tax return for the taxable year in which the sale of qualified securities occurred in any case in which any qualified replacement property was purchased by such time and during the qualified replacement period. If qualified replacement property was purchased after such filing date and during the qualified replacement period, the statement of purchase must be notarized not later than the time the taxpayer's income tax return is filed for the taxable year following the year for which the election under section 1042(a) was made.

#### **Proposed Effective Date**

The proposed amendments to the temporary regulations would apply to taxable years of sellers ending on or after the date of publication of the Treasury decision adopting these amendments as final regulations in the **Federal Register**. However, taxpayers may rely upon these proposed regulations for guidance with respect to all open taxable years pending the issuance of final regulations. If, and to the extent, future guidance is more restrictive than the guidance in these proposed regulations, the future guidance will be applied without retroactive effect.

#### **Special Analyses**

It has been determined that this notice of proposed rulemaking 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 a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Internal Revenue Code, these proposed regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

#### **Comments and Public Hearing**

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and 8 copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

#### **Drafting Information**

The principal author of these regulations is John T. Ricotta of the Office of the Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). However, other personnel from the IRS and Treasury participated in their development.

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

Income taxes, Reporting and recordkeeping requirements.

#### **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 continues to read in part as follows:

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

**Par. 2.** In § 1.1042-1T, A-3, in the undesignated paragraph following paragraph (b)(6), the penultimate