

utes money or other property to another partner and that partner recognizes gain or loss on the distribution or the basis of the property distributed to that partner is adjusted, the remaining partners' inside basis and outside basis may not be equal.

\* \* \*

\* \* \* \* \*

(b) \* \* \*

(2) *Required adjustments relating to distributions.* (i) This paragraph (b)(2) applies in situations where a corporation owns a direct or indirect interest in a partnership that owns stock in that corporation, the partnership distributes money or other property to another partner and that partner recognizes gain or loss on the distribution or the basis of the property distributed to that partner is adjusted during a year in which the partnership does not have an election under section 754 in effect, and the partnership subsequently sells or exchanges the stock. In these situations, the increase (or decrease) in the corporation's adjusted basis in its partnership interest resulting from the sale or exchange of the stock equals the amount of gain (or loss) that the corporate partner would have recognized (absent the application of section 1032) if, for the year in which the partnership made the distribution, a section 754 election had been in effect.

(ii) The provisions of this paragraph (b)(2) are illustrated by the following example:

*Example.* (i) A, B, and corporation C form partnership PRS. A and B each contribute \$10,000 and C contributes \$20,000 in exchange for a partnership interest. PRS has no liabilities. PRS purchases stock in corporation C for \$10,000, which appreciates in value to \$70,000. PRS distributes \$25,000 to A in complete liquidation of A's interest in PRS in a year for which an election under section 754 is not in effect. PRS later sells the C stock for \$70,000. PRS realizes a gain of \$60,000 on the sale of the C stock. C's share of the gain is \$40,000. Under section 1032, C does not recognize its share of the gain.

(ii) Normally, C would be entitled to a \$40,000 increase in the basis of its PRS interest for its allocable share of PRS's gain from the sale of the C stock, but a special rule applies in this situation. If a section 754 election had been in effect for the year in which PRS made the distribution to A, PRS would have been entitled to adjust the basis of partnership property under section 734(b)(1)(A) by \$15,000 (the amount of gain recognized by A with respect to the distribution to A under section 731(a)(1)). See §1.734-1(b). Under §1.755-1(c)(1)(ii), the basis adjustment under section 734(b) would have been allocated to the C stock, increasing its basis to \$25,000 (where there is a distribution resulting in an adjustment under sec-

tion 734(b)(1)(A) to the basis of undistributed partnership property, the adjustment is allocated only to capital gain property).

(iii) If a section 754 election had been in effect for the year in which PRS made the distribution to A, the amount of gain that PRS would have recognized upon PRS's disposition of C stock would be \$45,000 (\$70,000 minus \$25,000 basis in the C stock), and the amount of gain C would have recognized upon PRS's disposition of the C stock (absent the application of section 1032) would be \$30,000 (C's share of PRS's gain of \$45,000 from the stock sale). Accordingly, upon PRS's sale of the C stock, the increase in the basis of C's interest in PRS is \$30,000.

(c) \* \* \* (1) \* \* \* Similarly, if a corporation owns an indirect interest in its own stock through a chain of two or more partnerships, and a partnership in the chain distributes money or other property to another partner and that partner recognizes gain or loss on the distribution or the basis of the property distributed to that partner is adjusted during a year in which the partnership does not have an election under section 754 in effect, then upon any subsequent sale or exchange of the stock, the bases of the interests in the partnerships included in the chain shall be adjusted in a manner that is consistent with the purpose of this section.

\* \* \* \* \*

(d) *Positions in Stock.* For purposes of this section, stock includes any position in stock to which section 1032 applies.

(e) *Effective date.* This section applies to gain or loss allocated with respect to sales or exchanges of stock occurring after December 6, 1999, except that paragraph (d) of this section is applicable with respect to sales or exchanges of stock occurring on or after March 29, 2002, and the fourth sentence of paragraph (a), paragraph (b)(2), and the third sentence of paragraph (c)(1) of this section are applicable with respect to sales or exchanges of stock occurring on or after March 18, 2003.

David A. Mader,  
*Assistant Deputy Commissioner  
of Internal Revenue.*

Approved March 6, 2003.

Pamela F. Olson,  
*Assistant Secretary of the Treasury.*

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## Section 807.—Rules for Certain Reserves

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of April 2003. See Rev. Rul. 2003-35, on this page.

## Section 846.—Discounted Unpaid Losses Defined

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of April 2003. See Rev. Rul. 2003-35, on this page.

## Section 1033.—Involuntary Conversions

*26 CFR 1.1033(a)-1: Involuntary conversions; nonrecognition of gain.*

May a business defer, under section 1033, recognition of gain realized on receipt of a grant payment made under the World Trade Center grant program? See Notice 2003-18, page 699.

## Section 1274.—Determination of Issue Price in the Case of Certain Debt Instruments Issued for Property

*(Also Sections 42, 280G, 382, 412, 467, 468, 482, 483, 642, 807, 846, 1288, 7520, 7872.)*

**Federal rates; adjusted federal rates; adjusted federal long-term rate and the long-term exempt rate.** For purposes of sections 382, 1274, 1288, and other sections of the Code, tables set forth the rates for April 2003.

## Rev. Rul. 2003-35

This revenue ruling provides various prescribed rates for federal income tax purposes for April 2003 (the current month). Table 1 contains the short-term, mid-term, and long-term applicable federal rates (AFR) for the current month for purposes of section 1274(d) of the Internal Revenue Code. Table 2 contains the short-term, mid-term, and long-term adjusted applicable federal rates (adjusted AFR) for the current month for purposes of section

1288(b). Table 3 sets forth the adjusted federal long-term rate and the long-term tax-exempt rate described in section 382(f). Table 4 contains the appropriate percentages for determining the low-income hous-

ing credit described in section 42(b)(2) for buildings placed in service during the current month. Finally, Table 5 contains the federal rate for determining the present value of annuity, an interest for life or for

a term of years, or a remainder or a reversionary interest for purposes of section 7520.

REV. RUL. 2003-35 TABLE 1				
Applicable Federal Rates (AFR) for April 2003				
	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
<i>Short-Term</i>				
AFR	1.46%	1.45%	1.45%	1.45%
110% AFR	1.61%	1.60%	1.60%	1.59%
120% AFR	1.75%	1.74%	1.74%	1.73%
130% AFR	1.90%	1.89%	1.89%	1.88%
<i>Mid-Term</i>				
AFR	2.96%	2.94%	2.93%	2.92%
110% AFR	3.26%	3.23%	3.22%	3.21%
120% AFR	3.56%	3.53%	3.51%	3.50%
130% AFR	3.86%	3.82%	3.80%	3.79%
150% AFR	4.46%	4.41%	4.39%	4.37%
175% AFR	5.22%	5.15%	5.12%	5.10%
<i>Long-Term</i>				
AFR	4.58%	4.53%	4.50%	4.49%
110% AFR	5.04%	4.98%	4.95%	4.93%
120% AFR	5.51%	5.44%	5.40%	5.38%
130% AFR	5.98%	5.89%	5.85%	5.82%

REV. RUL. 2003-35 TABLE 2				
Adjusted AFR for April 2003				
	<i>Period for Compounding</i>			
	<i>Annual</i>	<i>Semiannual</i>	<i>Quarterly</i>	<i>Monthly</i>
<i>Short-term</i>				
adjusted AFR	1.26%	1.26%	1.26%	1.26%
<i>Mid-term</i>				
adjusted AFR	2.57%	2.55%	2.54%	2.54%
<i>Long-term</i>				
adjusted AFR	4.41%	4.36%	4.34%	4.32%

REV. RUL. 2003-35 TABLE 3

Rates Under Section 382 for April 2003

Adjusted federal long-term rate for the current month	4.41%
Long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months.)	4.58%

REV. RUL. 2003-35 TABLE 4

Appropriate Percentages Under Section 42(b)(2) for April 2003

Appropriate percentage for the 70% present value low-income housing credit	7.87%
Appropriate percentage for the 30% present value low-income housing credit	3.37%

REV. RUL. 2003-35 TABLE 5

Rate Under Section 7520 for April 2003

Applicable federal rate for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest	3.6%
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## Section 1288.—Treatment of Original Issue Discounts on Tax-Exempt Obligations

The adjusted applicable federal short-term, mid-term, and long-term rates are set forth for the month of April 2003. See Rev. Rul. 2003-35, page 687.

## Section 4945.—Taxes on Taxable Expenditures

26 CFR 53.4945-4: Grants to individuals. (Also §117; §1.117-1.)

**Scholarship grants, employer-related private foundations.** This ruling states that for purposes of sections 117 and 4945 of the Code, scholarships and educational grants awarded by a private foundation under an employer-related program to employees and their children, when the employee is a victim killed or seriously injured in a qualified disaster, may be awarded without regard to the percentage guidelines in Rev. Proc.

76-47, 1976-2 C.B. 670. Thus, grants awarded under such a program will be described in section 4945(g)(1) and will not be taxable expenditures under section 4945(d)(3).

### Rev. Rul. 2003-32

#### ISSUE

If a private foundation awards educational grants to employees or children of employees of a particular employer who are victims of a qualified disaster as defined in § 139 of the Internal Revenue Code, and the educational grants do not satisfy the percentage test of Rev. Proc. 76-47, 1976-2 C.B. 670, are these educational grants treated as scholarships subject to the provisions of § 117 and not treated as taxable expenditures under § 4945(d)(3)?

#### FACTS

The foundation is exempt from federal income tax under § 501(c)(3) and is a private foundation under § 509(a). The foundation has applied under § 4945(g) for

approval of its proposed scholarship program. The foundation intends to provide scholarships to employees or children of employees of a particular employer if the employee is seriously injured or killed as a result of a qualified disaster within the meaning of § 139(c)(1), (2), or (3). The foundation will determine whether these criteria are satisfied using objective standards that are consistently applied.

Section 139(c) provides that the term “qualified disaster” includes (1) a disaster that results from a terroristic or military action (as defined in § 692(c)), (2) a Presidentially declared disaster (as defined in § 1033(h)(3)), or (3) a disaster that results from an accident involving a common carrier, or from any other event, which is determined by the Secretary to be of a catastrophic nature.

The group of employees or children of employees from whom grantees are selected is sufficiently broad to constitute a charitable class. The foundation’s scholarship program will satisfy the requirements of § 4945(g)(1) and the guidelines of