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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 17

[TD 9546]

RIN 1545-BD04

Definition of Solid Waste Disposal Facilities for Tax-Exempt Bond Purposes

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations on the definition of solid waste disposal facilities for purposes of the rules applicable to tax-exempt bonds issued by State and local governments. These regulations provide guidance to State and local governments that issue tax-exempt bonds to finance solid waste disposal facilities and to taxpayers that use those facilities.

DATES: Effective Date: These regulations are effective August 19, 2011.

Applicability Date: For dates of applicability, see §1.142(a)(6)-1(i).

FOR FURTHER INFORMATION CONTACT: Timothy Jones, (202) 622-3980 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document amends the Income Tax Regulations (26 CFR part 1) under section 142 of the Internal Revenue Code (Code) to provide final rules for determining whether a facility is a solid waste disposal facility under section 142(a)(6). This document also removes certain

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existing regulations on this subject. On September 16, 2009, the IRS published a Notice of Proposed Rulemaking (REG-140492-02) in the **Federal Register** (74 FR 47500) (the Proposed Regulations). The Proposed Regulations under proposed §1.142(a)(6)-1 would modify existing regulations under §1.103-8(f)(2) of the Income Tax Regulations and §17.1 of the temporary Income Tax Regulations (together, the Existing Regulations) on this subject. Public comments on the Proposed Regulations were received and a public hearing was held on January 5, 2010.

After consideration of the public comments, the IRS and the Treasury Department adopt the Proposed Regulations, with revisions, as final regulations by this Treasury decision (the Final Regulations). Significant aspects of the public comments and the revisions made in the Final Regulations are discussed in this preamble.

Explanation of Provisions

1. Introduction.

In general, interest on State or local bonds is excludable from gross income under section 103(a). Under section 103(b), however, interest on private activity bonds is excludable from gross income under section 103 only if the bond meets the requirements for a qualified bond under section 141(e) and other applicable requirements under section 103. Section 141(e) defines a qualified bond to include an exempt facility bond that meets certain requirements. Section 142(a) defines an exempt facility bond to mean any bond that is issued as part of an issue 95 percent or more of the net proceeds of which are to be used to provide an exempt facility specified in section 142(a). Section 142(a)(6) includes a solid waste disposal facility as one specified type of qualified exempt facility.

In general, the Proposed Regulations addressed the requirements for solid waste disposal facilities under section 142(a)(6) for purposes of eligibility for tax-exempt private activity bond

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financing. The Proposed Regulations provided that a facility qualifies as a solid waste disposal facility if it processes solid waste in a qualified solid waste disposal process, performs preliminary functions, or is a functionally related or subordinate facility. The Proposed Regulations focused on eligible processes to dispose of solid waste, including a final disposal process, an energy conversion process, and a recycling process. The Proposed Regulations also provided a more developed definition of solid waste which focused on used materials and residual materials, with certain specific exclusions. The Proposed Regulations eliminated a "no-value" test from the solid waste definition under §1.103-8(f)(2)(ii)(b) of the Existing Regulations, which provides that material does not qualify as solid waste unless, on the issue date of the tax-exempt bonds used to provide the solid waste disposal facility, the property is useless, unused, unwanted, or discarded solid material "that has no market or other value at the place where the property is located" (No-Value Test). The Proposed Regulations also proposed various allocation and accounting rules based on existing principles for mixed-input facilities and mixed-use facilities. Overall, the Proposed Regulations implement a policy in favor of recycling through the use of solid waste disposal facilities.

Commentators generally supported the approach taken towards solid waste disposal facilities under the Proposed Regulations. The Final Regulations retain the overall approach of the Proposed Regulations and make certain technical changes in response to public comments, as discussed further in this preamble.

2. Solid Waste Disposal Facility.

The Proposed Regulations defined the term solid waste disposal facility to mean a facility that processes solid waste in a qualified solid waste disposal process, performs a preliminary

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function, or is a functionally related and subordinate facility. The Final Regulations retain this definition of a solid waste disposal facility.

3. Definition of Solid Waste.

The Proposed Regulations defined the term solid waste to mean garbage, refuse, and other solid material derived from any agricultural, commercial, consumer, or industrial operation or activity, based largely on an existing definition under the Existing Regulations. The Proposed Regulations refined the existing definition to require that solid waste be either used material or residual material. The Proposed Regulations also eliminated the No-Value Test. Additionally, the Proposed Regulations required that the person who acquires the material must reasonably expect to introduce it into a qualified solid waste disposal process within a reasonable period of time after acquisition.

The Proposed Regulations defined used material to mean any material that has been used previously as an agricultural, commercial, consumer, or industrial product or as a component of any such product. The Proposed Regulations defined residual material to mean any residual byproduct or excess unused raw material that remains from the production of any agricultural, commercial, consumer, or industrial product, provided that material qualified as residual material only to the extent that it constituted less than five percent (5%) of the total material introduced into the production process and it had a fair market value that is reasonably expected to be lower than that of any product made in that production process.

The Final Regulations generally retain the core definition of solid waste from the Proposed Regulations but modify that definition in certain technical respects. The Final Regulations clarify that material is "solid" only if it is solid at ambient temperature and pressure.

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The Final Regulations also clarify that solid waste can result from governmental operations or activities. The Final Regulations expand the definition of solid waste to include animal waste.

With respect to the definition of residual material, commentators generally supported the analytic standard under the Proposed Regulations but recommended removing the five percent (5%) size limitation on residual material. Commentators recommended removing this size limit because it unduly restricts the scope of residual material in many circumstances and it arbitrarily treats various industries and activities differently because residual amounts vary widely by industry and activity. The Final Regulations adopt this comment to eliminate the five percent (5%) size limitation on residual material and otherwise generally retain the analytic standard for residual material. The Final Regulations also expand the definition of residual material to include material derived from providing a service in which no product is produced.

Further, for purposes of determining residual material when multiple production processes are operated on the same site, commentators recommended a separate evaluation of each process. Based on reasons associated with scope and administrability, the IRS and the Treasury Department intended to cover only residual material that remains at the end of integrated processes that are functionally interconnected or interdependent, based on all the facts and circumstances. Accordingly, the Final Regulations do not adopt this comment. Instead, the Final Regulations adopt an integrated process standard to limit residual material.

4. Specific Exclusions from the Definition of Solid Waste.

In general, the Proposed Regulations excluded from the definition of solid waste the following items: (1) virgin material; (2) solids within liquids and liquid waste; (3) precious metals; (4) hazardous material; and (5) radioactive material. The Final Regulations retain these exclusions with certain technical modifications.

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The exclusion for virgin material aimed to distinguish solid waste disposal from manufacturing. The exclusion for certain precious metals aimed to recognize that recovery of these metals generally would take place without regard to a recycling industry. With respect to the exclusions for hazardous and radioactive waste, the statute and legislative history indicate that Congress intended to exclude hazardous waste and radioactive waste from solid waste. The statute treats qualified hazardous waste facilities as eligible exempt facilities under section 142(a)(10) separate and apart from solid waste disposal facilities under section 142(a)(6). In addition, the legislative history provides, in relevant part, that "the conferees wish to clarify that solid waste does not include most hazardous waste (including radioactive waste)." H.Rep. No. 99-841, at II-704 (1986), 1986-3 (Vol. 4) CB 704.

Some commentators expressed concern that the introduction of virgin material or precious metals into a final disposal process, such as a landfill (as contrasted with a recycling process), could disqualify a facility from treatment as a qualified solid waste disposal facility. The Final Regulations address this comment favorably and modify the definition of solid waste to allow the introduction of virgin materials and precious metals into a final disposal process. The Final Regulations also add a provision that allows the IRS to identify other excluded precious metals in future public administrative guidance.

Commentators also recommended treating hazardous waste and radioactive waste as solid waste. The Final Regulations generally do not adopt this comment. The IRS and the Treasury Department believe that Congress generally intended to exclude these materials from the definition of solid waste. Recognizing that only certain hazardous waste and radioactive waste are required to be disposed of at regulated facilities, however, the Final Regulations limit

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the exclusions for these two types of waste to the extent that they are required to be disposed of or contained at a regulated hazardous waste or radioactive waste disposal facility.

5. Qualified Solid Waste Disposal Process.

The Proposed Regulations provided for three eligible types of solid waste disposal processes: a final disposal process, an energy conversion process, and a recycling process. To provide flexibility for future innovation, the Proposed Regulations provided that, absent an express restriction in the proposed regulations, a solid waste disposal function may employ any biological, engineering, industrial, or technological method.

The Final Regulations generally retain the eligible types of solid waste disposal processes from the Proposed Regulations, with technical clarifications. The Final Regulations clarify that a final disposal process includes the spreading of solid waste in an environmentally compliant and safe manner. The Final Regulations also clarify that an energy conversion process ends at the point at which useful energy is first created or incorporated into the form of synthesis gas, heat, hot water, or other useful energy.

6. First Useful Product Principle.

The Propcsed Regulations provided guidance on the standard for determining the first useful product for purposes of establishing the end point of a solid waste disposal process. The first useful product principle has particular application to recycling. Under the Proposed Regulations, a useful product generally included a product useful for consumption, either as an ultimate end-use product or as an input to some stage of a manufacturing or production process, and that could be sold for such use (taking into account operational constraints on such sales for certain integrated processes), whether or not actually sold.

The Final Regulations generally retain the first useful product standard from the

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Proposed Regulations. Some commentators recommended that determinations under the first useful product rule take into account geographic location and transportation costs in certain situations. The Final Regulations adopt this comment.

7. Mixed-Input Facilities.

The Proposed Regulations provided a mixed-input accounting rule, which treated a facility as a qualified solid waste disposal facility if at least 65 percent of all of the material introduced into such facility in each year consisted of solid waste. This proposed rule recognizes that recycling processes may require supplemental inputs besides solid waste to operate viably. This proposed rule is similar to an existing rule under §1.103-8(f)(2)(ii)(c) of the Existing Regulations. This proposed rule requires annual testing for compliance with the requisite 65 percent solid waste threshold. Several commentators recommended reformulating this 65 percent test to require compliance based on an aggregate testing period measured over the life of the tax-exempt bonds instead of an annual testing period. These commentators expressed concerns about compliance with an annual test during start-up periods and aberrational years for various reasons.

The Final Regulations retain the annual 65 percent test for mixed-input facilities with modifications. In response to the public comments, the Final Regulations provide a special rule that allows a three-year curative period to address the impact of extraordinary events outside the control of the operator of the solid waste disposal facility (such as natural disasters, strikes, major utility disruptions, or governmental interventions). In addition, the Final Regulations provide that the annual testing does not begin until the facility is placed in service within the meaning of the special placed-in-service definition in §1.150-2(c), which focuses on the point at which a facility is operational at substantially its design level.

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8. Certain Other Changes.

Several commentators recommended removal of the proposed concept of facilities that perform a preliminary function for a qualified solid waste disposal process and removal of the threshold limit on preliminary functions that requires more than 50 percent of the materials that result from preliminary functions to constitute solid waste. The Final Regulations retain the concept of a preliminary function, but remove the 50 percent threshold limit on preliminary functions. The Final Regulations also provide for application of a mixed-use accounting rule to facilities that perform preliminary functions.

One commentator expressed concern that Example 2 in the Proposed Regulations was confusing, and the Final Regulations remove that example with no substantive inference intended by that removal. The Final Regulations also expand and clarify certain other examples.

Commentators recommended various transition rules for applicability of the Final Regulations to refunding bonds issued prior to the date of publication of the final regulations. The Final Regulations provide a transition rule for current refunding bonds the weighted average maturity of which is no longer than the remaining weighted average maturity of the refunded bonds.

Effective/Applicability Dates

The Final Regulations apply to bonds to which section 142 applies that are sold on or after October 18, 2011.

Issuers may apply the Final Regulations to outstanding bonds sold before October 18, 2011.

The Final Regulations need not be applied to bonds that are issued in a current

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refunding to refund bonds to which the Final Regulations do not apply if the weighted average maturity of the refunding bonds is no longer than the remaining weighted average maturity of the refunded bonds.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866, as supplemented by Executive Order 13563. 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 the regulations are interpretative and 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 Code, the proposed regulations preceding these final regulations were submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these final regulations is Timothy L. Jones, Office of Associate Chief Counsel (Financial Institutions and Products). However, other personnel from the IRS and the Treasury Department participated in their development.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 17

Income taxes, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

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Accordingly, under the authority of 26 U.S.C. 7805, 26 CFR parts 1 and 17 are 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 * * *

§1.103-8 [Amended]

Par. 2. Section 1.103-8 is amended by removing paragraph (f)(2)(ii) and redesignating paragraph (f)(2)(iii) as (f)(2)(ii).

Par. 3. Section 1.142(a)(6)-1 is added to read as follows:

§1.142(a)(6)-1 Exempt facility bonds: solid waste disposal facilities.

(a) In general. This section defines the term solid waste disposal facility for purposes of section 142(a)(6).

(b) Solid waste disposal facility. The term solid waste disposal facility means a facility to the extent that the facility--

(1) Processes solid waste (as defined in paragraph (c) of this section) in a qualified solid waste disposal process (as defined in paragraph (d) of this section);

(2) Performs a preliminary function (as defined in paragraph (f) of this section); or

(3) Is functionally related and subordinate (within the meaning of §1.103-8(a)(3)) to a facility described in paragraph (b)(1) or (b)(2) of this section.

(c) Solid waste--(1) In general. Except to the extent excluded under paragraph (c)(2) of this section, for purposes of section 142(a)(6), the term solid waste means garbage, refuse, and other solid material derived from any agricultural, commercial, consumer, governmental, or industrial operation or activity if the material meets the requirements of both paragraph (c)(1)(i)

and paragraph (c)(1)(ii) of this section. For purposes of this section, material is solid if it is solid at ambient temperature and pressure.

(i) Used material or residual material. Material meets the requirements of this paragraph (c)(1)(i) if it is either used material (as defined in paragraph (c)(1)(i)(A)) of this section or residual material (as defined in paragraph (c)(1)(i)(B) of this section).

(A) Used material. The term used material means any material that is a product of any agricultural, commercial, consumer, governmental, or industrial operation or activity, or a component of any such product or activity, and that has been used previously. Used material also includes animal waste produced by animals from a biological process.

(B) Residual material. The term residual material means material that meets the requirements of this paragraph (c)(1)(i)(B). The material must be a residual byproduct or excess raw material that results from or remains after the completion of any agricultural, commercial, consumer, governmental, or industrial production process or activity or from the provision of any service. In the case of multiple processes constituting an integrated manufacturing or industrial process, the material must result from or remain after the completion of such integrated process. As of the issue date of the bonds used to finance the solid waste disposal facility, the material must be reasonably expected to have a fair market value that is lower than the value of all of the products made in that production process or lower than the value of the service that produces such residual material.

(ii) Reasonably expected introduction into a qualified solid waste disposal process. Material meets the requirements of this paragraph (c)(1)(ii) if it is reasonably expected by the person who generates, purchases, or otherwise acquires it to be introduced within a reasonable

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time after such generation, purchase or acquisition into a qualified solid waste disposal process described in paragraph (d) of this section.

(2) Exclusions from solid waste. The following materials do not constitute solid waste:

(i) Virgin material. Except to the extent that virgin material constitutes an input to a final disposal process or residual material, solid waste excludes any virgin material. The term virgin material means material that has not been processed into an agricultural, commercial, consumer, governmental, or industrial product, or a component of any such product. Further, for this purpose, material continues to be virgin material after it has been grown, harvested, mined, or otherwise extracted from its naturally occurring location and cleaned, divided into component elements, modified, or enhanced, as long as further processing is required before it becomes an agricultural, commercial, consumer, or industrial product, or a component of any such product.

(ii) Solids within liquids and liquid waste. Solid waste excludes any solid or dissolved material in domestic sewage or other significant pollutant in water resources, such as silt, dissolved or suspended solids in industrial waste water effluents, dissolved materials in irrigation return flows or other common water pollutants, and liquid or gaseous waste.

(iii) Precious metals. Except to the extent that a precious metal constitutes an input to a final disposal process and/or an unrecoverable trace of the particular precious metal, solid waste excludes gold, silver, ruthenium, rhodium, palladium, osmium, iridium, platinum, gallium, rhenium, and any other precious metal material as may be identified by the Internal Revenue Service in future public administrative guidance.

(iv) Hazardous material. Solid waste excludes any hazardous material that must be disposed of at a facility that is subject to final permit requirements under subtitle C of title II of the Solid Waste Disposal Act as in effect on the date of the enactment of the Tax Reform Act of

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1986 (which is October 22, 1986). See section 142(h)(1) of the Internal Revenue Code for the definition of qualified hazardous waste facilities.

(v) Radioactive material. Solid waste excludes any radioactive material subject to regulation under the Nuclear Regulatory Act (10 CFR §1.1 et. seq), as in effect on the issue date of the bonds.

(d) Qualified solid waste disposal process. The term qualified solid waste disposal process means the processing of solid waste in a final disposal process (as defined in paragraph (d)(1) of this section), an energy conversion process (as defined in paragraph (d)(2) of this section), or a recycling process (as defined in paragraph (d)(3) of this section). Absent an express restriction to the contrary in this section, a qualified solid waste disposal process may employ any biological, engineering, industrial, or technological method.

(1) Final disposal process. The term final disposal process means the placement of solid waste in a landfill (including, for this purpose, the spreading of solid waste over land in an environmentally compliant and safe manner with no intent to remove such solid waste), the incineration of solid waste without capturing any useful energy, or the containment of solid waste with a reasonable expectation as of the date of issue of the bonds that the containment will continue indefinitely and that the solid waste has no current or future beneficial use.

(2) Energy conversion process. The term energy conversion process means a thermal, chemical, or other process that is applied to solid waste to create and capture synthesis gas, heat, hot water, steam, or other useful energy. The energy conversion process begins at the point of the first application of such process. The energy conversion process ends at the point at which the useful energy is first created, captured, or incorporated into the form of synthesis gas, heat, hot water, or other useful energy and before any transfer or distribution of such synthesis gas,

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heat, hot water or other useful energy, regardless of whether such synthesis gas, heat, hot water, or other useful energy constitutes a first useful product within the meaning of paragraph (e) of this section.

(3) Recycling process--(i) In general. The term recycling process means reconstituting, transforming, or otherwise processing solid waste into a useful product. The recycling process begins at the point of the first application of a process to reconstitute or transform the solid waste into a useful product, such as decontamination, melting, re-pulping, shredding, or other processing of the solid waste to accomplish this purpose. The recycling process ends at the point of completion of production of the first useful product from the solid waste.

(ii) Refurbishment, repair, or similar activities. The term recycling process does not include refurbishment, repair, or similar activities. The term refurbishment means the breakdown and reassembly of a product if such activity is done on a product-by-product basis and if the finished product contains more than 30 percent of its original materials or components.

(e) First useful product. The term first useful product means the first product produced from the processing of solid waste in a solid waste disposal process that is useful for consumption in agricultural, consumer, commercial, governmental, or industrial operation or activity and that could be sold for such use, whether or not actually sold. A useful product includes both a product useful to an individual consumer as an ultimate end-use consumer product and a product useful to an industrial user as a material or input for processing in some stage of a manufacturing or production process to produce a different end-use consumer product. The determination of whether a useful product has been produced may take into account operational constraints that affect the point in production when a useful product reasonably can be extracted or isolated and sold independently. For this purpose, the costs of extracting,

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isolating, storing, and transporting the product to a market may only be taken into account as operational constraints if the product is not to be used as part of an integrated manufacturing or industrial process in the same location as that in which the product is produced.

(f) Preliminary function. A preliminary function is a function to collect, separate, sort, store, treat, process, disassemble, or handle solid waste that is preliminary to and directly related to a qualified solid waste disposal process.

(g) Mixed-use facilities--(1) In general. If a facility is used for both a qualified solid waste disposal function (including a qualified solid waste disposal process or a preliminary function) and a nonqualified function (a mixed-use facility), then the costs of the facility allocable to the qualified solid waste disposal function are determined using any reasonable method, based on all the facts and circumstances. See §1.103-8(a)(1) for allocation rules on amounts properly allocable to an exempt facility. Facilities qualify as functionally related and subordinate to a qualified solid waste disposal function only to the extent that they are functionally related and subordinate to the portion of the mixed-use facility that is used for one or more qualified solid waste disposal functions (including a qualified solid waste disposal process or a preliminary function).

(2) Mixed inputs--(i) In general. Except as otherwise provided in paragraph (g)(2)(ii) of this section, for each facility (or a portion of a mixed-use facility) performing a qualified solid waste disposal process or a preliminary function, the percentage of the costs of the property used for such process that are allocable to a qualified solid waste disposal process or a preliminary function cannot exceed the average annual percentage of solid waste processed in that qualified solid waste disposal process or that preliminary function while the issue is outstanding. The annual percentage of solid waste processed in that qualified solid waste disposal process or

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preliminary function for any year is the percentage, by weight or volume, of the total materials processed in that qualified solid waste disposal process or preliminary function that constitute solid waste for that year.

(ii) Special rule for mixed-input processes if at least 65 percent of the materials processed are solid waste--(A) In general. Except as otherwise provided in paragraph (g)(2)(ii)(B) of this section, for each facility (or a portion of a mixed-use facility) performing a qualified solid waste disposal process or preliminary function, if the annual percentage of solid waste processed in that qualified solid waste disposal process or preliminary function for each year that the issue is outstanding (beginning with the date such facility is placed in service within the meaning of §1.150-2(c)) equals at least 65 percent of the materials processed in that qualified solid waste disposal process or preliminary function, then all of the costs of the property used for such process are treated as allocable to a qualified solid waste disposal process. The annual percentage of solid waste processed in such qualified solid waste disposal process or preliminary function for any year is the percentage, by weight or volume, of the total materials processed in that qualified solid waste disposal process or preliminary function that constitute solid waste for that year.

(B) Special rule for extraordinary events. In the case of an extraordinary event that is beyond the control of the operator of a solid waste disposal facility (such as a natural disaster, strike, major utility disruption, or governmental intervention) and that causes a solid waste disposal facility to be unable to meet the 65 percent test under paragraph (g)(2)(ii)(A) of this section for a particular year, the percentage of solid waste processed for that year equals--

(1) The sum of the amount of solid waste processed in the solid waste disposal facility for the year affected by the extraordinary event and the amount of solid waste processed in the solid

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waste disposal facility during the following two years in excess of the amount required to meet the general 65 percent threshold for the facility during each of such two years; divided by

(2) The total materials processed in the solid waste disposal facility during the year affected by the extraordinary event. If the resulting measure of solid waste processed for the year affected by the extraordinary event equals at least 65 percent, then the facility is treated as meeting the requirements of the 65 percent test under paragraph (g)(2)(ii)(A) of this section for such year.

(iii) Facilities functionally related and subordinate to mixed-input facilities. Except to the extent that facilities are functionally related and subordinate to a mixed-input facility that meets the 65 percent test under paragraph (g)(2)(ii) of this section, facilities qualify as functionally related and subordinate to a mixed-input facility only to the extent that they are functionally related and subordinate to the qualified portion of the mixed-input facility that is used for one or more qualified solid waste disposal functions (including a qualified solid waste disposal process or a preliminary function).

(h) Examples. The following examples illustrate the application of this section:

Example 1. Nonqualified Unused Material--Cloth. Company A takes wool and weaves it into cloth and then sells the cloth to a manufacturer to manufacture clothing. The cloth is material that has not been used previously as a product of or otherwise used in an agricultural, commercial, consumer, governmental, or industrial operation or activity, or as a component of any such product or activity. Accordingly, the cloth is not solid waste.

Example 2. Residual Material--Waste Coal. Company B mines coal. Some of the ore mined is a low quality byproduct of coal mining commonly known as waste coal, which cannot be converted to energy under a normal energy-production process because the BTU content is too low. Waste coal has the lowest fair market value of any product produced in Company B's coal mining process. Waste coal is solid waste because it is residual material within the meaning of paragraph (c)(1)(i)(B) of this section and Company B reasonably expects to introduce the waste coal into a solid waste disposal process.

Example 3. Virgin Material--Logs. Company C cuts down trees and sells the logs to another company, which further processes the logs into lumber. In order to facilitate shipping,

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Company C cuts the trees into uniform logs. The trees are not solid waste because they are virgin material within the meaning of paragraph (c)(2)(i) of this section that are not being introduced into a final disposal process within the meaning of paragraph (d)(1) of this section. The division of such trees into uniform logs does not change the status of the trees as virgin material.

Example 4. Qualified Solid Waste Disposal Process--Landfill. Company D plans to construct a landfill. The landfill will not be subject to the final permit requirements under subtitle C of title II of the Solid Waste Disposal Act (as in effect on the date of enactment of the Tax Reform Act of 1986). As of the issue date, Company D expects that the landfill will be filled entirely with material that will qualify as solid waste within the meaning of paragraph (c) of this section. Placing solid waste into a landfill is a qualified solid waste disposal process. The landfill is a qualified solid waste disposal facility.

Example 5. Qualified Solid Waste Disposal Process--Recycling Tires. Company E owns a facility that converts used tires into roadbed material. The used tires are used material within the meaning of paragraph (c)(1)(i)(A) of this section that qualifies as solid waste. Between the introduction of the old tires into the roadbed manufacturing process and the completion of the roadbed material, the facility does not create any interim useful products. The process for the manufacturing of the roadbed material from the old tires is a qualified solid waste disposal process as a recycling process and the facility that converts the tires into roadbed material is a qualified solid waste disposal facility. This conclusion would be the same if the recycling process took place at more than one plant.

Example 6. Qualified Solid Waste Disposal Process--Energy Conversion Process. Company F receives solid waste from a municipal garbage collector. Company F burns that solid waste in an incinerator to remove exhaust gas and to produce heat. Company F further processes the heat in a heat exchanger to produce steam. Company F further processes the steam to generate electricity. The energy conversion process ends with the production of steam. The facilities used to burn the solid waste and to capture the steam as useful energy are qualified solid waste disposal facilities because they process solid waste in an energy conversion process. The generating facilities used to process the steam further to generate electricity are not engaged in the energy conversion process and are not qualified solid waste disposal facilities.

Example 7. Nonqualified Refurbishment. Company G purchases used cars and restores them. This restoration process includes disassembly, cleaning, and repairing of the cars. Parts that cannot be repaired are replaced. The restored cars contain at least 30 percent of the original parts. While the cars are used material, the refurbishing process is not a qualified solid waste disposal process. Accordingly, Company G's facility is not a qualified solid waste disposal facility.

Example 8. Qualified Solid Waste Disposal Facility--First Useful Product Rule--Paper Recycling. (i) Company H employs an integrated process to re-pulp discarded magazines, clean the pulp, and produce retail paper towel products. Operational constraints on Company H's process do not allow for reasonable extraction, isolation, and sale of the cleaned paper pulp independently without degradation of the pulp. Company H further processes the paper pulp into

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large industrial-sized rolls of paper which are approximately 12 feet in diameter. At this point in the process, Company H could either sell such industrial-sized rolls of paper to another company for further processing to produce retail paper products or it could produce those retail products itself. In general, paper pulp is a useful product that is bought and sold on the market as a material for input into manufacturing or production processes. The discarded magazines are used material within the meaning of paragraph (c)(1)(i)(A) of this section. Company H's facility is engaged in a recycling process within the meaning of paragraph (d)(3) of this section to the extent that it repulps and cleans the discarded magazines generally and further to the extent that it produces industrial-sized rolls of paper under the particular circumstances here. Specifically, taking into account the operational constraints on Company H's facility that limit its ability reasonably to extract, isolate, and sell the paper pulp independently, the first useful products within the meaning of paragraph (e) of this section from Company H's recycling process are the industrial-sized rolls of paper. The portion of Company H's facility that processes the discarded magazines and produces industrial-sized rolls of paper is a qualified solid waste disposal facility, and the portion of Company H's facility that further processes the industrial-sized rolls of paper into retail paper towels is not a qualified solid waste facility.

(ii) The facts are the same as in paragraph (i) of this Example 8, except that Company H is able reasonably to extract the cleaned paper pulp from the process without degradation of the pulp and to sell the cleaned paper pulp at its dock for a price that exceeds its costs of extracting the pulp from the process. Therefore, the paper pulp is the first useful product within the meaning of paragraph (e) of this section. As a result, the portion of Company H's facility that processes the discarded magazines is a qualified solid waste disposal facility, and the portion of Company H's facility that produces industrial-sized rolls of paper is not a qualified solid waste disposal facility. If, however, the only reasonable way Company H could sell the pulp was to transport the pulp to a distant market, then the costs of storing and transporting the pulp to the market may be taken into account in determining whether the pulp is the first useful product.

Example 9. Preliminary Function--Energy Conversion Process. (i) Company I owns a paper mill. At the mill, logs from nearby timber operations are processed through a machine that removes bark. The stripped logs are used to manufacture paper. The stripped bark has the lowest fair market value of any product produced from the paper mill. The stripped bark falls onto a conveyor belt that transports the bark to a storage bin that is used to store the bark briefly until Company I feeds the bark into a boiler. The conveyor belt and storage bin are used only for these purposes. The boiler is used only to create steam by burning the bark, and the steam is used to generate electricity. The stripped bark is solid waste because it is residual material within the meaning of paragraph (c)(1)(i)(B) of this section and Company I expects to introduce the bark into an energy conversion process within a reasonable period of time. The creation of steam from the stripped bark is an energy conversion process that starts with the incineration of the stripped bark. The energy conversion process is a qualified solid waste disposal process. The conveyor belt performs a collection activity that is preliminary and that is directly related to the solid waste disposal function. The storage bin performs a storage function that is preliminary and that is directly related to the solid waste disposal function. Thus, the conveyor belt and storage bin are solid waste disposal facilities. The bark removal process is not a preliminary function because it is not directly related to the energy conversion process and it does not become so related merely because it results in material that is solid waste.

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(ii) The facts are the same as in paragraph (a) of this Example 9, except that the stripped bark represents only 55 percent by weight and volume of the materials that are transported by the conveyor belt. The remaining 45 percent of the materials transported by the conveyor belt are not solid waste and these other materials are sorted from the conveyor belt by a sorting machine immediately before the stripped bark arrives at the storage bin. Fifty-five percent of the costs of the conveyor belt and the sorting machine are allocable to solid waste disposal functions.

Example 10. Preliminary Function--Final Disposal Process. Company J owns a waste transfer station and uses it to collect, sort, and process solid waste. Company J uses its trucks to haul the solid waste to the nearest landfill. At least 65 percent by weight and volume of the material brought to the transfer station is solid waste. The waste transfer station and the trucks perform functions that are preliminary and directly related to the solid waste disposal function of the landfill. Thus, the waste transfer station and the trucks qualify as solid waste disposal facilities.

Example 11. Mixed-Input Facility. Company K owns an incinerator financed by an issue and uses the incinerator exclusively to burn coal and other solid material to create steam. Each year while the issue is outstanding, 40 percent by volume and 45 percent by weight of the solid material that Company K processes in the conversion process is coal. The remainder of the solid material is either used material or residual material within the meaning of paragraph (c)(1)(i) of this section. Sixty percent of the costs of the property used to perform the energy conversion process are allocable to a solid waste disposal function.

(i) Effective/Applicability Dates--(1) In general. Except as otherwise provided in this paragraph (i), this section applies to bonds to which section 142 applies that are sold on or after October 18, 2011.

(2) Elective retroactive application. Issuers may apply this section, in whole, but not in part, to outstanding bonds to which section 142 applies and which were sold before October 18, 2011.

(3) Certain refunding bonds. An issuer need not apply this section to bonds that are issued in a current refunding to refund bonds to which this section does not apply if the weighted average maturity of the refunding bonds is no longer than the remaining weighted average maturity of the refunded bonds.

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PART 17--**[Removed]**

Par. 4. Part 17 is removed.

Steven T. Miller,
Deputy Commissioner for Services and Enforcement.

Approved by: August 9, 2011.

Emily S. McMahon,
(Acting) Assistant Secretary of the Treasury (Tax Policy).

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