

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-357 applicable to amounts paid or incurred after Oct. 22, 2004, see section 902(d) of Pub. L. 108-357, set out as a note under section 195 of this title.

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(a)(36) of Pub. L. 94-455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94-455, set out as a note under section 2 of this title.

Amendment by section 1906(b)(13)(A) of Pub. L. 94-455 effective Feb. 1, 1977, see section 1906(d)(1) of Pub. L. 94-455, set out as a note under section 6013 of this title.

§ 249. Limitation on deduction of bond premium on repurchase

(a) General rule

No deduction shall be allowed to the issuing corporation for any premium paid or incurred upon the repurchase of a bond, debenture, note, or certificate or other evidence of indebtedness which is convertible into the stock of the issuing corporation, or a corporation in control of, or controlled by, the issuing corporation, to the extent the repurchase price exceeds an amount equal to the adjusted issue price plus a normal call premium on bonds or other evidences of indebtedness which are not convertible. The preceding sentence shall not apply to the extent that the corporation can demonstrate to the satisfaction of the Secretary that such excess is attributable to the cost of borrowing and is not attributable to the conversion feature.

(b) Special rules

For purposes of subsection (a)—

(1) Adjusted issue price

The adjusted issue price is the issue price (as defined in sections 1273(b) and 1274) increased by any amount of discount deducted before repurchase, or, in the case of bonds or other evidences of indebtedness issued after February 28, 1913, decreased by any amount of premium included in gross income before repurchase by the issuing corporation.

(2) Control

The term “control” has the meaning assigned to such term by section 368(c).

(Added Pub. L. 91-172, title IV, §414(a), Dec. 30, 1969, 83 Stat. 612; amended Pub. L. 94-455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 98-369, div. A, title I, §42(a)(5), July 18, 1984, 98 Stat. 557.)

AMENDMENTS

1984—Subsec. (b)(1). Pub. L. 98-369 substituted “sections 1273(b) and 1274” for “section 1232(b)”.

1976—Subsec. (a). Pub. L. 94-455 struck out “or his delegate” after “Secretary”.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by Pub. L. 98-369 applicable to taxable years ending after July 18, 1984, see section 44 of Pub. L. 98-369, set out as an Effective Date note under section 1271 of this title.

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by Pub. L. 94-455 effective Feb. 1, 1977, see section 1906(d)(1) of Pub. L. 94-455, set out as a note under section 6013 of this title.

EFFECTIVE DATE

Section 414(c) of Pub. L. 91-172, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that: “The amendments made by this section [enacting this section] shall apply to a convertible bond or other convertible evidence of indebtedness repurchased after April 22, 1969, other than such a bond or other evidence of indebtedness repurchased pursuant to a binding obligation incurred on or before April 22, 1969, to repurchase such bond or other evidence of indebtedness at a specified call premium, but no inference shall be drawn from the fact that section 249 of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (as added by subsection (a) of this section) does not apply to the repurchase of such convertible bond or other convertible evidence of indebtedness.”

[§ 250. Repealed. Pub. L. 101-508, title XI, § 11801(a)(15), Nov. 5, 1990, 104 Stat. 1388-520]

Section, added Pub. L. 91-518, title IX, §901(a), Oct. 30, 1970, 84 Stat. 1341; amended Pub. L. 93-496, §12, Oct. 28, 1974, 88 Stat. 1531; Pub. L. 94-455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 95-473, §2(a)(2)(C), Oct. 17, 1978, 92 Stat. 1464; Pub. L. 96-454, §3(b)(1), Oct. 15, 1980, 94 Stat. 2012; Pub. L. 97-261, §6(d)(3), Sept. 20, 1982, 96 Stat. 1107; Pub. L. 99-521, §4(3), Oct. 22, 1986, 100 Stat. 2993, related to certain payments to National Railroad Passenger Corporation.

SAVINGS PROVISION

For provisions that nothing in repeal by Pub. L. 101-508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101-508, set out as a note under section 45K of this title.

PART IX—ITEMS NOT DEDUCTIBLE

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[280.	Repealed.]

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AMENDMENTS

1996—Pub. L. 104-188, title I, §1704(t)(55), Aug. 20, 1996, 110 Stat. 1890, provided that section 11813(b)(13)(F) of Pub. L. 101-508 shall be applied as if “tax” appeared after “investment” in the material proposed to be stricken. See 1990 Amendment note below.

1990—Pub. L. 101-508, title XI, §11813(b)(13)(F), Nov. 5, 1990, 104 Stat. 1388-555, which directed the striking out of “investment credit and” in item 280F, was executed by striking out “investment tax credit and” after “Limitation on”. See 1996 Amendment note above.

1988—Pub. L. 100-418, title I, §1941(b)(4)(B), Aug. 23, 1988, 102 Stat. 1324, struck out item 280D “Portion of chapter 45 taxes for which credit or refund is allowable under section 6429”.

1987—Pub. L. 100-203, title X, §10206(c)(2), Dec. 22, 1987, 101 Stat. 1330-402, added item 280H.

1986—Pub. L. 99-514, title VIII, §803(c)(1), (3), Oct. 22, 1986, 100 Stat. 2356, added item 263A and struck out items 278 “Capital expenditures incurred in planting and developing citrus and almond groves” and 280 “Certain expenditures incurred in production of films, books, records, or similar property”.

1984—Pub. L. 98-369, div. A, title I, §§67(d)(1), 136(b), 179(c), title X, §1063(b)(2), July 18, 1984, 98 Stat. 587, 670, 718, 1047, added items 269B, 280F, and 280G, and struck out “certain historic” before “structures” in item 280B.

1983—Pub. L. 97-414, §4(b)(2)(B), Jan. 4, 1983, 96 Stat. 2056, substituted “Certain expenses for which credits are allowable” for “Portion of wages for which credit is claimed under section 44B” in item 280C.

1982—Pub. L. 97-248, title II, §250(b), title III, §351(b), Sept. 3, 1982, 96 Stat. 528, 640, added items 269A and 280E.

1980—Pub. L. 96-499, title XI, §1131(d)(2), Dec. 5, 1980, 94 Stat. 2693, added item 280D.

1977—Pub. L. 95-30, title II, §202(c)(2), May 23, 1977, 91 Stat. 147, added item 280C.

1976—Pub. L. 94-455, title II, §210(b), title VI, §601(b), title XXI, §2124(b)(2), Oct. 4, 1976, 90 Stat. 1544, 1572, 1918, added items 280, 280A, and 280B.

1971—Pub. L. 91-680, §1(c), Jan. 12, 1971, 84 Stat. 2064, inserted “and almond” after “citrus” in item 278.

1969—Pub. L. 91-172, title I, §121(b)(3)(B), title II, §§213(c)(2), 216(b), title IV, §411(b), Dec. 30, 1969, 83 Stat. 541, 572, 574, 608, struck out item 270 “Limitation on deductions allowable to individuals in certain cases”, and added items 277 to 279.

1966—Pub. L. 89-368, title III, §301(b), Mar. 15, 1966, 80 Stat. 67, added item 276.

1964—Pub. L. 88-272, title II, §§207(b)(3)(B), 227(b)(4), Feb. 26, 1964, 78 Stat. 42, 98, inserted “or domestic iron ore” in item 272, and added item 275.

1962—Pub. L. 87-834, §4(a)(2), Oct. 16, 1962, 76 Stat. 976, added item 274.

§ 261. General rule for disallowance of deductions

In computing taxable income no deduction shall in any case be allowed in respect of the items specified in this part.

¹ So in original. Does not conform to section catchline.

(Aug. 16, 1954, ch. 736, 68A Stat. 76.)

§ 262. Personal, living, and family expenses

(a) General rule

Except as otherwise expressly provided in this chapter, no deduction shall be allowed for personal, living, or family expenses.

(b) Treatment of certain phone expenses

For purposes of subsection (a), in the case of an individual, any charge (including taxes thereon) for basic local telephone service with respect to the 1st telephone line provided to any residence of the taxpayer shall be treated as a personal expense.

(Aug. 16, 1954, ch. 736, 68A Stat. 76; Pub. L. 100-647, title V, §5073(a), Nov. 10, 1988, 102 Stat. 3682.)

AMENDMENTS

1988—Pub. L. 100-647 amended section generally. Prior to amendment, section read as follows: “Except as otherwise expressly provided in this chapter, no deduction shall be allowed for personal, living, or family expenses.”

EFFECTIVE DATE OF 1988 AMENDMENT

Section 5073(b) of Pub. L. 100-647 provided that: “The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1988.”

§ 263. Capital expenditures

(a) General rule

No deduction shall be allowed for—

(1) Any amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate. This paragraph shall not apply to—

(A) expenditures for the development of mines or deposits deductible under section 616.

(B) research and experimental expenditures deductible under section 174.

(C) soil and water conservation expenditures deductible under section 175.

(D) expenditures by farmers for fertilizer, etc., deductible under section 180.

(E) expenditures for removal of architectural and transportation barriers to the handicapped and elderly which the taxpayer elects to deduct under section 190.

(F) expenditures for tertiary injectants with respect to which a deduction is allowed under section 193;¹

(G) expenditures for which a deduction is allowed under section 179;¹

(H) expenditures for which a deduction is allowed under section 179A.

(I) expenditures for which a deduction is allowed under section 179B.

(J) expenditures for which a deduction is allowed under section 179C.

(K) expenditures for which a deduction is allowed under section 179D, or

(L) expenditures for which a deduction is allowed under section 179E.

(2) Any amount expended in restoring property or in making good the exhaustion thereof for which an allowance is or has been made.

¹ So in original. The semicolon probably should be a comma.

[(b) Repealed. Pub. L. 101-508, title XI, § 11801(a)(16), Nov. 5, 1990, 104 Stat. 1388-520]

(c) Intangible drilling and development costs in the case of oil and gas wells and geothermal wells

Notwithstanding subsection (a), and except as provided in subsection (i), regulations shall be prescribed by the Secretary under this subtitle corresponding to the regulations which granted the option to deduct as expenses intangible drilling and development costs in the case of oil and gas wells and which were recognized and approved by the Congress in House Concurrent Resolution 50, Seventy-ninth Congress. Such regulations shall also grant the option to deduct as expenses intangible drilling and development costs in the case of wells drilled for any geothermal deposit (as defined in section 613(e)(2)) to the same extent and in the same manner as such expenses are deductible in the case of oil and gas wells. This subsection shall not apply with respect to any costs to which any deduction is allowed under section 59(e) or 291.

(d) Expenditures in connection with certain railroad rolling stock

In the case of expenditures in connection with the rehabilitation of a unit of railroad rolling stock (except a locomotive) used by a domestic common carrier by railroad which would, but for this subsection, be properly chargeable to capital account, such expenditures, if during any 12-month period they do not exceed an amount equal to 20 percent of the basis of such unit in the hands of the taxpayer, shall, at the election of the taxpayer, be treated (notwithstanding subsection (a)) as deductible repairs under section 162 or 212. An election under this subsection shall be made for any taxable year at such time and in such manner as the Secretary prescribes by regulations. An election may not be made under this subsection for any taxable year to which an election under subsection (e) applies to railroad rolling stock (other than locomotives).

[(e) Repealed. Pub. L. 97-34, title II, § 201(c), Aug. 13, 1981, 95 Stat. 219]

(f) Railroad ties

In the case of a domestic common carrier by rail (including a railroad switching or terminal company) which uses the retirement-replacement method of accounting for depreciation of its railroad track, expenditures for acquiring and installing replacement ties of any material (and fastenings related to such ties) shall be accorded the same tax accounting treatment as expenditures for replacement ties of wood (and fastenings related to such ties).

(g) Certain interest and carrying costs in the case of straddles

(1) General rule

No deduction shall be allowed for interest and carrying charges properly allocable to personal property which is part of a straddle (as defined in section 1092(c)). Any amount not allowed as a deduction by reason of the preceding sentence shall be chargeable to the capital account with respect to the personal property to which such amount relates.

(2) Interest and carrying charges defined

For purposes of paragraph (1), the term “interest and carrying charges” means the excess of—

(A) the sum of—

(i) interest on indebtedness incurred or continued to purchase or carry the personal property, and

(ii) all other amounts (including charges to insure, store, or transport the personal property) paid or incurred to carry the personal property, over

(B) the sum of—

(i) the amount of interest (including original issue discount) includible in gross income for the taxable year with respect to the property described in subparagraph (A),

(ii) any amount treated as ordinary income under section 1271(a)(3)(A), 1276, or 1281(a) with respect to such property for the taxable year,

(iii) the excess of any dividends includible in gross income with respect to such property for the taxable year over the amount of any deduction allowable with respect to such dividends under section 243, 244, or 245, and

(iv) any amount which is a payment with respect to a security loan (within the meaning of section 512(a)(5)) includible in gross income with respect to such property for the taxable year.

For purposes of subparagraph (A), the term “interest” includes any amount paid or incurred in connection with personal property used in a short sale.

(3) Exception for hedging transactions

This subsection shall not apply in the case of any hedging transaction (as defined in section 1256(e)).

(4) Application with other provisions

(A) Subsection (c)

In the case of any short sale, this subsection shall be applied after subsection (h).

(B) Section 1277 or 1282

In the case of any obligation to which section 1277 or 1282 applies, this subsection shall be applied after section 1277 or 1282.

(h) Payments in lieu of dividends in connection with short sales

(1) In general

If—

(A) a taxpayer makes any payment with respect to any stock used by such taxpayer in a short sale and such payment is in lieu of a dividend payment on such stock, and

(B) the closing of such short sale occurs on or before the 45th day after the date of such short sale,

then no deduction shall be allowed for such payment. The basis of the stock used to close the short sale shall be increased by the amount not allowed as a deduction by reason of the preceding sentence.

(2) Longer period in case of extraordinary dividends

If the payment described in paragraph (1)(A) is in respect of an extraordinary dividend, paragraph (1)(B) shall be applied by substituting “the day 1 year after the date of such short sale” for “the 45th day after the date of such short sale”.

(3) Extraordinary dividend

For purposes of this subsection, the term “extraordinary dividend” has the meaning given to such term by section 1059(c); except that such section shall be applied by treating the amount realized by the taxpayer in the short sale as his adjusted basis in the stock.

(4) Special rule where risk of loss diminished

The running of any period of time applicable under paragraph (1)(B) (as modified by paragraph (2)) shall be suspended during any period in which—

(A) the taxpayer holds, has an option to buy, or is under a contractual obligation to buy, substantially identical stock or securities, or

(B) under regulations prescribed by the Secretary, a taxpayer has diminished his risk of loss by holding 1 or more other positions with respect to substantially similar or related property.

(5) Deduction allowable to extent of ordinary income from amounts paid by lending broker for use of collateral**(A) In general**

Paragraph (1) shall apply only to the extent that the payments or distributions with respect to any short sale exceed the amount which—

(i) is treated as ordinary income by the taxpayer, and

(ii) is received by the taxpayer as compensation for the use of any collateral with respect to any stock used in such short sale.

(B) Exception not to apply to extraordinary dividends

Subparagraph (A) shall not apply if one or more payments or distributions is in respect of an extraordinary dividend.

(6) Application of this subsection with subsection (g)

In the case of any short sale, this subsection shall be applied before subsection (g).

(i) Special rules for intangible drilling and development costs incurred outside the United States

In the case of intangible drilling and development costs paid or incurred with respect to an oil, gas, or geothermal well located outside the United States—

(1) subsection (c) shall not apply, and

(2) such costs shall—

(A) at the election of the taxpayer, be included in adjusted basis for purposes of computing the amount of any deduction allowable under section 611 (determined without regard to section 613), or

(B) if subparagraph (A) does not apply, be allowed as a deduction ratably over the 10-taxable year period beginning with the taxable year in which such costs were paid or incurred.

This subsection shall not apply to costs paid or incurred with respect to a nonproductive well.

(Aug. 16, 1954, ch. 736, 68A Stat. 77; Pub. L. 86-779, § 6(c), Sept. 14, 1960, 74 Stat. 1001; Pub. L. 87-834, § 21(b), Oct. 16, 1962, 76 Stat. 1064; Pub. L. 88-563, § 4, Sept. 2, 1964, 78 Stat. 845; Pub. L. 89-243, § 4(p)(1), (2), Oct. 9, 1965, 79 Stat. 964; Pub. L. 91-172, title VII, § 706(a), Dec. 30, 1969, 83 Stat. 674; Pub. L. 92-178, title I, § 109(b), (c), Dec. 10, 1971, 85 Stat. 509; Pub. L. 94-455, title XVII, § 1701(a), title XIX, §§ 1904(b)(10)(A)(i), 1906(b)(13)(A), title XXI, § 2122(b)(2), Oct. 4, 1976, 90 Stat. 1759, 1817, 1834, 1915; Pub. L. 95-618, title IV, § 402(a), Nov. 9, 1978, 92 Stat. 3201; Pub. L. 96-223, title II, § 251(a)(2)(B), Apr. 2, 1980, 94 Stat. 287; Pub. L. 97-34, title II, §§ 201(c), 202(d)(1), title V, § 502, Aug. 13, 1981, 95 Stat. 219, 221, 327; Pub. L. 97-248, title II, § 204(c)(1), Sept. 3, 1982, 96 Stat. 426; Pub. L. 97-448, title I, § 105(b)(1), title III, § 306(a)(9)(A), Jan. 12, 1983, 96 Stat. 2385, 2403; Pub. L. 98-369, div. A, title I, §§ 56(a), 102(e)(7), (8), July 18, 1984, 98 Stat. 573, 624, 625; Pub. L. 99-514, title IV, §§ 402(b)(1), 411(b)(1), title VII, § 701(e)(4)(D), title XVIII, § 1808(b), Oct. 22, 1986, 100 Stat. 2221, 2225, 2343, 2817; Pub. L. 100-647, title I, § 1007(g)(5), Nov. 10, 1988, 102 Stat. 3435; Pub. L. 101-508, title XI, §§ 11801(a)(16), 11815(b)(3), Nov. 5, 1990, 104 Stat. 1388-520, 1388-558; Pub. L. 105-34, title XVI, § 1604(a)(1), Aug. 5, 1997, 111 Stat. 1097; Pub. L. 108-311, title IV, § 408(a)(10), Oct. 4, 2004, 118 Stat. 1191; Pub. L. 108-357, title III, § 338(b)(1), Oct. 22, 2004, 118 Stat. 1481; Pub. L. 109-58, title XIII, §§ 1323(b)(2), 1331(b)(4), Aug. 8, 2005, 119 Stat. 1015, 1024; Pub. L. 109-432, div. A, title IV, § 404(b)(1), Dec. 20, 2006, 120 Stat. 2956.)

AMENDMENTS

2006—Subsec. (a)(1)(L). Pub. L. 109-432 added subpar. (L).

2005—Subsec. (a)(1)(J). Pub. L. 109-58, § 1323(b)(2), added subpar. (J).

Subsec. (a)(1)(K). Pub. L. 109-58, § 1331(b)(4), added subpar. (K).

2004—Subsec. (a)(1)(I). Pub. L. 108-357 added subpar. (I).

Subsec. (g)(2)(B)(ii). Pub. L. 108-311 substituted “1276” for “1278”.

1997—Subsec. (a)(1)(H). Pub. L. 105-34 added subpar. (H).

1990—Subsec. (b). Pub. L. 101-508, § 11801(a)(16), struck out subsec. (b) “Expenditures for advertising and good will” which read as follows: “If a corporation has, for the purpose of computing its excess profits tax credit under chapter 2E or subchapter D of chapter 1 of the Internal Revenue Code of 1939 claimed the benefits of the election provided in section 733 or section 451 of such code, as the case may be, no deduction shall be allowable under section 162 to such corporation for expenditures for advertising or the promotion of good will which, under the rules and regulations prescribed under section 733 or section 451 of such code, as the case may be, may be regarded as capital investments.”

Subsec. (c). Pub. L. 101-508, § 11815(b)(3), substituted “section 613(e)(2)” for “section 613(e)(3)”.

1988—Subsec. (c). Pub. L. 100-647 substituted “section 59(e)” for “section 59(d)”.

1986—Subsec. (a)(1)(E) to (H). Pub. L. 99-514, § 402(b)(1), struck out subpar. (E) relating to non-

application of par. (1) to expenditures by farmers for clearing land deductible under section 182, and redesignated subpars. (F) to (H) as (E) to (G), respectively.

Subsec. (c). Pub. L. 99-514, § 701(e)(4)(D), substituted “59(d)” for “58(i)”.

Pub. L. 99-514, § 411(b)(1)(B), inserted “and except as provided in subsection (i).”.

Subsec. (g)(2)(B)(iv). Pub. L. 99-541, § 1808(b), added cl. (iv).

Subsec. (i). Pub. L. 99-514, § 411(b)(1)(A), added subsec. (i).

1984—Subsec. (g)(2). Pub. L. 98-369, § 102(e)(7), amended par. (2) generally, striking out “charges for temporary use of the personal property in a short sale, or” after “(including” in subpar. (A)(ii), substituting “any amount treated as ordinary income under section 1271(a)(3)(A), 1278, or 1281(a) with respect to such property for the taxable year, and” for “any amount treated as ordinary income under section 1232(a)(3)(A) with respect to such property for the taxable year” in subpar. (B)(ii), and adding subpar. (B)(iii).

Subsec. (g)(4). Pub. L. 98-369, § 102(e)(8), added par. (4).

Subsec. (h). Pub. L. 98-369, § 56(a), added subsec. (h).

1983—Subsec. (g)(2)(A)(ii). Pub. L. 97-448, § 105(b)(1), substituted “all other amounts (including charges for temporary use of the personal property in a short sale, or to insure, store, or transport the personal property) paid or incurred to carry the personal property, over” for “amounts paid or incurred to insure, store, or transport the personal property, over”.

Subsec. (g)(2)(B)(ii). Pub. L. 97-448, § 306(a)(9)(A), substituted “section 1232(a)(3)(A)” for “section 1232(a)(4)(A)”.

1982—Subsec. (c). Pub. L. 97-248, § 204(c)(1), inserted provision that this subsection not apply with respect to any costs to which any deduction is allowed under section 58(i) or 291.

1981—Subsec. (a)(1)(H). Pub. L. 97-34, § 202(d)(1), added subpar. (H).

Subsec. (e). Pub. L. 97-34, § 201(c), struck out subsec. (e) which related to the allowance of repair expenses or specified repair, rehabilitation, or improvement expenditures.

Subsec. (g). Pub. L. 97-34, § 502, added subsec. (g).

1980—Subsec. (a)(1)(G). Pub. L. 96-223 added subpar. (G).

1978—Subsec. (c). Pub. L. 95-618 inserted “and geothermal wells” after “gas wells” in heading and in text inserted provision that such regulations also grant the option to deduct as expenses intangible drilling and development costs in the case of wells drilled for any geothermal deposit (as defined in section 613(e)(3)) to the same extent and in the same manner as such expenses are deductible in the case of oil and gas wells.

1976—Subsec. (a)(1)(F). Pub. L. 94-455, § 2122(b)(2), added subpar. (F).

Subsec. (a)(3). Pub. L. 94-455, § 1904(b)(10)(A)(i)(I), struck out par. (3) which provided that no deduction be allowed for amounts paid as tax under section 4911 (relating to imposition of interest equalization tax) except as provided in subsec. (d).

Subsec. (d). Pub. L. 94-455, §§ 1904(b)(10)(A)(i)(I), (II), 1906(b)(13)(A), redesignated subsec. (e) as (d) and struck out “or his delegate” after “Secretary” and substituted “subsection (e)” for “subsection (f)”. Former subsec. (d) was struck out.

Subsec. (e). Pub. L. 94-455, §§ 1904(b)(10)(A)(i)(I), 1906(b)(13)(A), redesignated subsec. (f) as (e) and struck out “or his delegate” after “Secretary”. Former subsec. (e) redesignated (d).

Subsec. (f). Pub. L. 94-455, §§ 1701(a), 1904(b)(10)(A)(i)(I), added subsec. (f). Former subsec. (f) redesignated (e).

1971—Subsec. (e). Pub. L. 92-178, § 109(c), substituted “shall, at the election of the taxpayer, be treated” for “shall be treated” and inserted provisions respecting making of election under this subsection for any taxable year at such time and in such manner as Secretary or his delegate prescribed by regulation and prohibiting making of election for any taxable year to which an

election under subsec. (f) applies to railroad rolling stock (other than locomotives).

Subsec. (f). Pub. L. 92-178, § 109(b), added subsec. (f).

1969—Subsec. (e). Pub. L. 91-172 added subsec. (e).

1965—Subsec. (a)(3). Pub. L. 89-243, § 4(p)(1), inserted “Except as provided in subsection (d)”, and struck out “except to the extent that any amount attributable to the amount paid as tax is included in gross income for the taxable year” after parenthetical provision.

Subsec. (d). Pub. L. 89-243, § 4(p)(2), added subsec. (d).

1964—Subsec. (a)(3). Pub. L. 88-563 added par. (3).

1962—Subsec. (a)(1)(E). Pub. L. 87-834 added subpar. (E).

1960—Subsec. (a)(1)(D). Pub. L. 86-779 added subpar. (D).

EFFECTIVE DATE OF 2006 AMENDMENT

Amendment by Pub. L. 109-432 applicable to costs paid or incurred after Dec. 20, 2006, see section 404(c) of Pub. L. 109-432, set out as an Effective Date note under section 179E of this title.

EFFECTIVE DATE OF 2005 AMENDMENT

Amendment by section 1323(b)(2) of Pub. L. 109-58 applicable to properties placed in service after Aug. 8, 2005, see section 1323(c) of Pub. L. 109-58, set out as an Effective Date note under section 179C of this title.

Amendment by section 1331(b)(4) of Pub. L. 109-58 applicable to property placed in service after Dec. 31, 2005, see section 1331(d) of Pub. L. 109-58, set out as an Effective Date note under section 179D of this title.

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-357 applicable to expenses paid or incurred after Dec. 31, 2002, in taxable years ending after such date, see section 338(c) of Pub. L. 108-357, set out as an Effective Date note under section 179B of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Section 1604(a)(4) of Pub. L. 105-34 provided that: “The amendments made by this subsection [amending this section and sections 312 and 1245 of this title] shall take effect as if included in the amendments made by section 1913 of the Energy Policy Act of 1992 [Pub. L. 102-486].”

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 402(b)(1) of Pub. L. 99-514 applicable to amounts paid or incurred after Dec. 31, 1985, in taxable years ending after such date, see section 402(c) of Pub. L. 99-514 set out as an Effective Date of Repeat note under former section 182 of this title.

Section 411(c) of Pub. L. 99-514 provided that:

“(1) IN GENERAL.—The amendments made by this section [amending this section and sections 243, 291, 381, 616, and 617 of this title] shall apply to costs paid or incurred after December 31, 1986, in taxable years ending after such date.

“(2) TRANSITION RULE.—The amendments made by this section shall not apply with respect to intangible drilling and development costs incurred by United States companies pursuant to a minority interest in a license for Netherlands or United Kingdom North Sea development if such interest was acquired on or before December 31, 1985.”

Amendment by section 701(e)(4)(D) of Pub. L. 99-514 applicable to taxable years beginning after Dec. 31, 1986, with certain exceptions and qualifications, see section 701(f) of Pub. L. 99-514, set out as an Effective Date note under section 55 of this title.

Amendment by section 1808(b) of Pub. L. 99-514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98-369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99-514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 56(a) of Pub. L. 98-369 applicable to short sales after July 18, 1984, in taxable years ending after that date, see section 56(d) of Pub. L. 98-369, set out as a note under section 163 of this title.

Amendment by section 102(e)(7), (8) of Pub. L. 98-369 applicable to positions established after July 18, 1984, in taxable years ending after that date, except as otherwise provided, see section 102(f), (g) of Pub. L. 98-369, set out as a note under section 1256 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Section 105(b)(2) of Pub. L. 97-448 provided that: "The amendment made by paragraph (1) [amending this section] shall apply to property acquired, and positions established, by the taxpayer after September 22, 1982, in taxable years ending after such date."

Amendment by section 306 of Pub. L. 97-448 effective as if included in the provisions of the Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. 97-248, to which such amendment relates, see section 311(d) of Pub. L. 97-448, set out as a note under section 31 of this title.

EFFECTIVE DATE OF 1982 AMENDMENT

Amendment by Pub. L. 97-248 applicable to taxable years beginning after December 31, 1982, see section 204(d)(1) of Pub. L. 97-248, set out as an Effective Date note under section 291 of this title.

EFFECTIVE DATE OF 1981 AMENDMENT

Amendment by sections 201(c) and 202(d)(1) of Pub. L. 97-34 applicable to property placed in service after Dec. 31, 1980, in taxable years ending after that date, see section 209(a) of Pub. L. 97-34, set out as an Effective Date note under section 168 of this title.

Amendment by section 502 of Pub. L. 97-34 applicable to property acquired and positions established by the taxpayer after June 23, 1981, in taxable years ending after such date, and applicable when so elected with respect to property held on June 23, 1981, see section 508 of Pub. L. 97-34, set out as an Effective Date note under section 1092 of this title.

EFFECTIVE DATE OF 1980 AMENDMENT

Amendment by Pub. L. 96-223 applicable to taxable years beginning after Dec. 31, 1979, see section 251(b) of Pub. L. 96-223, set out as an Effective Date note under section 193 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Section 402(e) of Pub. L. 95-618, as amended by Pub. L. 99-514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that: "(1) IN GENERAL.—The amendments made by this section [amending this section and sections 57, 465, 751, and 1254 of this title] shall apply with respect to wells commenced on or after October 1, 1978, in taxable years ending on or after such date.

"(2) ELECTION.—The taxpayer may elect to capitalize or deduct any costs to which section 263(c) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] applies by reason of the amendments made by this section [amending this section and sections 57, 465, 751, and 1254 of this title]. Any such election shall be made before the expiration of the time for filing claim for credit or refund of any overpayment of tax imposed by chapter 1 of such Code [section 1 et seq. of this title] with respect to the taxpayer's first taxable year to which the amendments made by this section apply and for which he pays or incurs costs to which such section 263(c) applies by reason of the amendments made by this sec-

tion. Any election under this paragraph may be changed or revoked at any time before the expiration of the time referred to in the preceding sentence, but after the expiration of such time such election may not be changed or revoked."

EFFECTIVE DATE OF 1976 AMENDMENT

Section 1904(b)(10)(A)(vii) of Pub. L. 94-455 provided that: "The amendments made by this subparagraph [amending this section and sections 6011, 6611, and 6651 of this title and repealing sections 6076 and 6680 of this title] shall apply with respect to acquisitions of stock or debt obligations made after June 30, 1974, except that the repeal of paragraph (2) of section 6011(d) under clause (ii) shall apply with respect to loans and commitments made after such date."

Amendment by section 2122(b)(2) of Pub. L. 94-455, as amended by Pub. L. 96-167, § 9(c), Dec. 29, 1979, 93 Stat. 1278, applicable to taxable years beginning after Dec. 31, 1976, see section 2122(c) of Pub. L. 94-455, as amended, set out as an Effective Date note under section 190 of this title.

EFFECTIVE DATE OF 1971 AMENDMENT

Section 109(d)(2), (3) of Pub. L. 92-178 provided that: "(2) The amendment made by subsection (b) [amending this section] shall apply to taxable years ending after December 31, 1970.

"(3) The amendments made by subsection (c) [amending this section] shall apply to taxable years beginning after December 31, 1969."

EFFECTIVE DATE OF 1969 AMENDMENT

Section 706(b) of Pub. L. 91-172 provided that: "The amendment made by subsection (a) [amending this section] shall apply with respect to taxable years beginning after December 31, 1969."

EFFECTIVE DATE OF 1965 AMENDMENT

Section 4(p)(3) of Pub. L. 89-243 provided that: "The amendments made by this subsection [amending this section] shall apply to taxable years ending after September 2, 1964."

Section 4(q) of Pub. L. 89-243 provided in part that: "Except as otherwise specifically provided in this section and in the amendments made by this section [amending this section and sections 4912, 4914, 4916, 4917, 4919, 4920, and 4931 of this title], such amendments shall apply with respect to acquisitions of stock and debt obligations made after February 10, 1965."

EFFECTIVE DATE OF 1962 AMENDMENT

Section 21(d) of Pub. L. 87-834 provided that: "The amendments made by this section [enacting section 182 of this title and amending this section] shall apply with respect to taxable years beginning after December 31, 1962."

EFFECTIVE DATE OF 1960 AMENDMENT

Amendment by Pub. L. 86-779 applicable to taxable years beginning after Dec. 31, 1959, see section 6(d) of Pub. L. 86-779, set out as an Effective Date note under section 180 of this title.

SHORT TITLE OF 1965 AMENDMENT

Section 1(a) of Pub. L. 89-243 provided that: "This Act [amending this section and sections 4912, 4914, 4916, 4917, 4919, 4920, and 4931 of this title, and enacting provisions set out as notes under sections 6011 and 6076 of this title] may be cited as the 'Interest Equalization Tax Extension Act of 1965'."

SHORT TITLE OF 1964 AMENDMENT

Section 1(a) of Pub. L. 88-563 provided that: "This Act [enacting sections 4911 to 4920, 4931, 6076, 6680, 6681, and 7241 of this title, amending this section and sections 1232, 6011, and 6103 of this title, and enacting provisions set out as notes under section 6011 of this title] may be cited as the 'Interest Equalization Tax Act'."

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101-508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101-508, set out as a note under section 45K of this title.

APPLICABILITY OF CERTAIN AMENDMENTS BY PUB. L. 99-514 IN RELATION TO TREATY OBLIGATIONS OF UNITED STATES

For applicability of amendment by section 701(e)(4)(D) of Pub. L. 99-514 notwithstanding any treaty obligation of the United States in effect on Oct. 22, 1986, with provision that for such purposes any amendment by title I of Pub. L. 100-647 be treated as if it had been included in the provision of Pub. L. 99-514 to which such amendment relates, see section 1012(aa)(2), (4) of Pub. L. 100-647, set out as a note under section 861 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL
JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101-1147 and 1171-1177] or title XVIII [§§ 1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

§ 263A. Capitalization and inclusion in inventory costs of certain expenses**(a) Nondeductibility of certain direct and indirect costs****(1) In general**

In the case of any property to which this section applies, any costs described in paragraph (2)—

(A) in the case of property which is inventory in the hands of the taxpayer, shall be included in inventory costs, and

(B) in the case of any other property, shall be capitalized.

(2) Allocable costs

The costs described in this paragraph with respect to any property are—

(A) the direct costs of such property, and

(B) such property's proper share of those indirect costs (including taxes) part or all of which are allocable to such property.

Any cost which (but for this subsection) could not be taken into account in computing taxable income for any taxable year shall not be treated as a cost described in this paragraph.

(b) Property to which section applies

Except as otherwise provided in this section, this section shall apply to—

(1) Property produced by taxpayer

Real or tangible personal property produced by the taxpayer.

(2) Property acquired for resale**(A) In general**

Real or personal property described in section 1221(a)(1) which is acquired by the taxpayer for resale.

(B) Exception for taxpayer with gross receipts of \$10,000,000 or less

Subparagraph (A) shall not apply to any personal property acquired during any taxable year by the taxpayer for resale if the average annual gross receipts of the taxpayer (or any predecessor) for the 3-taxable year period ending with the taxable year preceding such taxable year do not exceed \$10,000,000.

(C) Aggregation rules, etc.

For purposes of subparagraph (B), rules similar to the rules of paragraphs (2) and (3) of section 448(c) shall apply.

For purposes of paragraph (1), the term "tangible personal property" shall include a film, sound recording, video tape, book, or similar property.

(c) General exceptions**(1) Personal use property**

This section shall not apply to any property produced by the taxpayer for use by the taxpayer other than in a trade or business or an activity conducted for profit.

(2) Research and experimental expenditures

This section shall not apply to any amount allowable as a deduction under section 174.

(3) Certain development and other costs of oil and gas wells or other mineral property

This section shall not apply to any cost allowable as a deduction under section 167(h), 179B, 263(c), 263(i), 291(b)(2), 616, or 617.

(4) Coordination with long-term contract rules

This section shall not apply to any property produced by the taxpayer pursuant to a long-term contract.

(5) Timber and certain ornamental trees

This section shall not apply to—

(A) trees raised, harvested, or grown by the taxpayer other than trees described in clause (ii) of subsection (e)(4)(B) (after application of the last sentence thereof), and

(B) any real property underlying such trees.

(6) Coordination with section 59(e)

Paragraphs (2) and (3) shall apply to any amount allowable as a deduction under section 59(e) for qualified expenditures described in subparagraphs (B), (C), (D), and (E) of paragraph (2) thereof.

(d) Exception for farming businesses**(1) Section not to apply to certain property****(A) In general**

This section shall not apply to any of the following which is produced by the taxpayer in a farming business:

(i) Any animal.

(ii) Any plant which has a preproductive period of 2 years or less.

(B) Exception for taxpayers required to use accrual method

Subparagraph (A) shall not apply to any corporation, partnership, or tax shelter re-

quired to use an accrual method of accounting under section 447 or 448(a)(3).

(2) Treatment of certain plants lost by reason of casualty

(A) In general

If plants bearing an edible crop for human consumption were lost or damaged (while in the hands of the taxpayer) by reason of freezing temperatures, disease, drought, pests, or casualty, this section shall not apply to any costs of the taxpayer of replanting plants bearing the same type of crop (whether on the same parcel of land on which such lost or damaged plants were located or any other parcel of land of the same acreage in the United States).

(B) Special rule for person with minority interest who materially participates

Subparagraph (A) shall apply to amounts paid or incurred by a person (other than the taxpayer described in subparagraph (A)) if—

(i) the taxpayer described in subparagraph (A) has an equity interest of more than 50 percent in the plants described in subparagraph (A) at all times during the taxable year in which such amounts were paid or incurred, and

(ii) such other person holds any part of the remaining equity interest and materially participates in the planting, maintenance, cultivation, or development of such the plants described in subparagraph (A) during the taxable year in which such amounts were paid or incurred.

The determination of whether an individual materially participates in any activity shall be made in a manner similar to the manner in which such determination is made under section 2032A(e)(6).

(3) Election to have this section not apply

(A) In general

If a taxpayer makes an election under this paragraph, this section shall not apply to any plant produced in any farming business carried on by such taxpayer.

(B) Certain persons not eligible

No election may be made under this paragraph by a corporation, partnership, or tax shelter, if such corporation, partnership, or tax shelter is required to use an accrual method of accounting under section 447 or 448(a)(3).

(C) Special rule for citrus and almond growers

An election under this paragraph shall not apply with respect to any item which is attributable to the planting, cultivation, maintenance, or development of any citrus or almond grove (or part thereof) and which is incurred before the close of the 4th taxable year beginning with the taxable year in which the trees were planted. For purposes of the preceding sentence, the portion of a citrus or almond grove planted in 1 taxable year shall be treated separately from the portion of such grove planted in another taxable year.

(D) Election

Unless the Secretary otherwise consents, an election under this paragraph may be made only for the taxpayer's 1st taxable year which begins after December 31, 1986, and during which the taxpayer engages in a farming business. Any such election, once made, may be revoked only with the consent of the Secretary.

(e) Definitions and special rules for purposes of subsection (d)

(1) Recapture of expensed amounts on disposition

(A) In general

In the case of any plant with respect to which amounts would have been capitalized under subsection (a) but for an election under subsection (d)(3)—

(i) such plant (if not otherwise section 1245 property) shall be treated as section 1245 property, and

(ii) for purposes of section 1245, the recapture amount shall be treated as a deduction allowed for depreciation with respect to such property.

(B) Recapture amount

For purposes of subparagraph (A), the term "recapture amount" means any amount allowable as a deduction to the taxpayer which, but for an election under subsection (d)(3), would have been capitalized with respect to the plant.

(2) Effects of election on depreciation

(A) In general

If the taxpayer (or any related person) makes an election under subsection (d)(3), the provisions of section 168(g)(2) (relating to alternative depreciation) shall apply to all property of the taxpayer used predominantly in the farming business and placed in service in any taxable year during which any such election is in effect.

(B) Related person

For purposes of subparagraph (A), the term "related person" means—

(i) the taxpayer and members of the taxpayer's family,

(ii) any corporation (including an S corporation) if 50 percent or more (in value) of the stock of such corporation is owned (directly or through the application of section 318) by the taxpayer or members of the taxpayer's family,

(iii) a corporation and any other corporation which is a member of the same controlled group described in section 1563(a)(1), and

(iv) any partnership if 50 percent or more (in value) of the interests in such partnership is owned directly or indirectly by the taxpayer or members of the taxpayer's family.

(C) Members of family

For purposes of this paragraph, the term "family" means the taxpayer, the spouse of the taxpayer, and any of their children who

have not attained age 18 before the close of the taxable year.

(3) Preproductive period

(A) In general

For purposes of this section, the term “preproductive period” means—

(i) in the case of a plant which will have more than 1 crop or yield, the period before the 1st marketable crop or yield from such plant, or

(ii) in the case of any other plant, the period before such plant is reasonably expected to be disposed of.

For purposes of this subparagraph, use by the taxpayer in a farming business of any supply produced in such business shall be treated as a disposition.

(B) Rule for determining period

In the case of a plant grown in commercial quantities in the United States, the preproductive period for such plant if grown in the United States shall be based on the nationwide weighted average preproductive period for such plant.

(4) Farming business

For purposes of this section—

(A) In general

The term “farming business” means the trade or business of farming.

(B) Certain trades and businesses included

The term “farming business” shall include the trade or business of—

(i) operating a nursery or sod farm, or

(ii) the raising or harvesting of trees bearing fruit, nuts, or other crops, or ornamental trees.

For purposes of clause (ii), an evergreen tree which is more than 6 years old at the time severed from the roots shall not be treated as an ornamental tree.

(5) Certain inventory valuation methods permitted

The Secretary shall by regulations permit the taxpayer to use reasonable inventory valuation methods to compute the amount required to be capitalized under subsection (a) in the case of any plant.

(f) Special rules for allocation of interest to property produced by the taxpayer

(1) Interest capitalized only in certain cases

Subsection (a) shall only apply to interest costs which are—

(A) paid or incurred during the production period, and

(B) allocable to property which is described in subsection (b)(1) and which has—

(i) a long useful life,

(ii) an estimated production period exceeding 2 years, or

(iii) an estimated production period exceeding 1 year and a cost exceeding \$1,000,000.

(2) Allocation rules

(A) In general

In determining the amount of interest required to be capitalized under subsection (a) with respect to any property—

(i) interest on any indebtedness directly attributable to production expenditures with respect to such property shall be assigned to such property, and

(ii) interest on any other indebtedness shall be assigned to such property to the extent that the taxpayer’s interest costs could have been reduced if production expenditures (not attributable to indebtedness described in clause (i)) had not been incurred.

(B) Exception for qualified residence interest

Subparagraph (A) shall not apply to any qualified residence interest (within the meaning of section 163(h)).

(C) Special rule for flow-through entities

Except as provided in regulations, in the case of any flow-through entity, this paragraph shall be applied first at the entity level and then at the beneficiary level.

(3) Interest relating to property used to produce property

This subsection shall apply to any interest on indebtedness allocable (as determined under paragraph (2)) to property used to produce property to which this subsection applies to the extent such interest is allocable (as so determined) to the produced property.

(4) Definitions

For purposes of this subsection—

(A) Long useful life

Property has a long useful life if such property is—

(i) real property, or

(ii) property with a class life of 20 years or more (as determined under section 168).

(B) Production period

The term “production period” means, when used with respect to any property, the period—

(i) beginning on the date on which production of the property begins, and

(ii) ending on the date on which the property is ready to be placed in service or is ready to be held for sale.

(C) Production expenditures

The term “production expenditures” means the costs (whether or not incurred during the production period) required to be capitalized under subsection (a) with respect to the property.

(g) Production

For purposes of this section—

(1) In general

The term “produce” includes construct, build, install, manufacture, develop, or improve.

(2) Treatment of property produced under contract for the taxpayer

The taxpayer shall be treated as producing any property produced for the taxpayer under a contract with the taxpayer; except that only costs paid or incurred by the taxpayer (whether under such contract or otherwise) shall be

taken into account in applying subsection (a) to the taxpayer.

(h) Exemption for free lance authors, photographers, and artists

(1) In general

Nothing in this section shall require the capitalization of any qualified creative expense.

(2) Qualified creative expense

For purposes of this subsection, the term “qualified creative expense” means any expense—

(A) which is paid or incurred by an individual in the trade or business of such individual (other than as an employee) of being a writer, photographer, or artist, and

(B) which, without regard to this section, would be allowable as a deduction for the taxable year.

Such term does not include any expense related to printing, photographic plates, motion picture films, video tapes, or similar items.

(3) Definitions

For purposes of this subsection—

(A) Writer

The term “writer” means any individual if the personal efforts of such individual create (or may reasonably be expected to create) a literary manuscript, musical composition (including any accompanying words), or dance score.

(B) Photographer

The term “photographer” means any individual if the personal efforts of such individual create (or may reasonably be expected to create) a photograph or photographic negative or transparency.

(C) Artist

(i) In general

The term “artist” means any individual if the personal efforts of such individual create (or may reasonably be expected to create) a picture, painting, sculpture, statue, etching, drawing, cartoon, graphic design, or original print edition.

(ii) Criteria

In determining whether any expense is paid or incurred in the trade or business of being an artist, the following criteria shall be taken into account:

(I) The originality and uniqueness of the item created (or to be created).

(II) The predominance of aesthetic value over utilitarian value of the item created (or to be created).

(D) Treatment of certain corporations

(i) In general

If—

(I) substantially all of the stock of a corporation is owned by a qualified employee-owner and members of his family (as defined in section 267(c)(4)), and

(II) the principal activity of such corporation is performance of personal services directly related to the activities of

the qualified employee-owner and such services are substantially performed by the qualified employee-owner,

this subsection shall apply to any expense of such corporation which directly relates to the activities of such employee-owner in the same manner as if such expense were incurred by such employee-owner.

(ii) Qualified employee-owner

For purposes of this subparagraph, the term “qualified employee-owner” means any individual who is an employee-owner of the corporation (as defined in section 269A(b)(2)) and who is a writer, photographer, or artist.

(i) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including—

(1) regulations to prevent the use of related parties, pass-thru entities, or intermediaries to avoid the application of this section, and

(2) regulations providing for simplified procedures for the application of this section in the case of property described in subsection (b)(2).

(Added Pub. L. 99-514, title VIII, § 803(a), Oct. 22, 1986, 100 Stat. 2350; amended Pub. L. 100-647, title I, § 1008(b)(1)-(4), title VI, § 6026(a)-(c), Nov. 10, 1988, 102 Stat. 3437, 3438, 3691-3693; Pub. L. 101-239, title VII, § 7816(d)(1), Dec. 19, 1989, 103 Stat. 2420; Pub. L. 106-170, title V, § 532(c)(2)(B), Dec. 17, 1999, 113 Stat. 1930; Pub. L. 108-357, title III, § 338(b)(2), Oct. 22, 2004, 118 Stat. 1481; Pub. L. 109-58, title XIII, § 1329(b), Aug. 8, 2005, 119 Stat. 1020).

AMENDMENTS

2005—Subsec. (c)(3). Pub. L. 109-58 inserted “167(h),” after “under section”.

2004—Subsec. (c)(3). Pub. L. 108-357, which directed amendment of par. (3) by inserting “179B,” after “section”, was executed by making the insertion after “section” the second place it appeared to reflect the probable intent of Congress.

1999—Subsec. (b)(2)(A). Pub. L. 106-170 substituted “1221(a)(1)” for “1221(1)”.

1989—Subsec. (h)(3)(D). Pub. L. 101-239 substituted “corporations” for “personal service corporations” in heading and amended text generally. Prior to amendment, text read as follows:

“(i) IN GENERAL.—In the case of a personal service corporation, this subsection shall apply to any expense of such corporation which directly relates to the activities of the qualified employee-owner in the same manner as if such expense were incurred by such employee-owner.

“(ii) QUALIFIED EMPLOYEE-OWNER.—The term ‘qualified employee-owner’ means any individual who is an employee-owner of the personal service corporation and who is a writer, photographer, or artist, but only if substantially all of the stock of such corporation is owned by such individual and members of his family (as defined in section 267(c)(4)).

“(iii) PERSONAL SERVICE CORPORATION.—For purposes of this subparagraph, the term ‘personal service corporation’ means any personal service corporation (as defined in section 269A(b)).”

1988—Subsec. (a)(2). Pub. L. 100-647, § 1008(b)(1), inserted at end “Any cost which (but for this subsection) could not be taken into account in computing taxable income for any taxable year shall not be treated as a cost described in this paragraph.”

Subsec. (c)(3). Pub. L. 100-647, §1008(b)(2)(A), substituted “section 263(c), 263(i), 291(b)(2), 616, or 617” for “section 263(c), 616(a), or 617(a)”.

Subsec. (c)(6). Pub. L. 100-647, §1008(b)(2)(B), added par. (6).

Subsec. (d)(1). Pub. L. 100-647, §6026(b)(2)(A), substituted “Section not to apply to certain property” for “Section to apply only if preproductive period is more than 2 years” in heading.

Subsec. (d)(1)(A). Pub. L. 100-647, §6026(b)(1), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: “This section shall not apply to any plant or animal which is produced by the taxpayer in a farming business and which has a preproductive period of 2 years or less.”

Subsec. (d)(2)(B)(i). Pub. L. 100-647, §1008(b)(3)(A), substituted “the plants described in subparagraph (A) at all times during the taxable year in which such amounts were paid or incurred” for “such grove, orchard, or vineyard”.

Subsec. (d)(2)(B)(ii). Pub. L. 100-647, §1008(b)(3)(B), substituted “the plants described in subparagraph (A) during the taxable year in which such amounts were paid or incurred” for “such grove, orchard, or vineyard during the 4-taxable year period beginning with the taxable year in which the grove, orchard, or vineyard was lost or damaged”.

Subsec. (d)(3)(A). Pub. L. 100-647, §6026(b)(2)(B), struck out “or animal” after “plant”.

Subsec. (d)(3)(B). Pub. L. 100-647, §6026(c), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: “No election may be made under this paragraph—

“(i) by a corporation, partnership, or tax shelter, if such corporation, partnership, or tax shelter is required to use an accrual method of accounting under section 447 or 448(a)(3), or

“(ii) with respect to the planting, cultivation, maintenance, or development of pistachio trees.”

Subsec. (e). Pub. L. 100-647, §6026(b)(2)(B), struck out “or animal” after “plant” wherever appearing in pars. (1), (3), and (5).

Subsec. (f)(3). Pub. L. 100-647, §1008(b)(4), substituted “allocable (as determined under paragraph (2)) to” for “incurred or continued in connection with” and inserted “(as so determined)” after “allocable”.

Subsecs. (h), (i). Pub. L. 100-647, §6026(a), added subsec. (h) and redesignated former subsec. (h) as (i).

EFFECTIVE DATE OF 2005 AMENDMENT

Amendment by Pub. L. 109-58 applicable to amounts paid or incurred in taxable years beginning after Aug. 8, 2005, see section 1329(c) of Pub. L. 109-58, set out as a note under section 167 of this title.

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-357 applicable to expenses paid or incurred after Dec. 31, 2002, in taxable years ending after such date, see section 338(c) of Pub. L. 108-357, set out as an Effective Date note under section 179B of this title.

EFFECTIVE DATE OF 1999 AMENDMENT

Amendment by Pub. L. 106-170 applicable to any instrument held, acquired, or entered into, any transaction entered into, and supplies held or acquired on or after Dec. 17, 1999, see section 532(d) of Pub. L. 106-170, set out as a note under section 170 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by Pub. L. 101-239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100-647, to which such amendment relates, see section 7817 of Pub. L. 101-239, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1008(b)(1)-(4) of Pub. L. 100-647 effective, except as otherwise provided, as if included in

the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

Section 6026(d) of Pub. L. 100-647, as amended by Pub. L. 101-239, title VII, §7816(d)(2), Dec. 19, 1989, 103 Stat. 2421, provided that:

“(1) IN GENERAL.—Except as otherwise provided in this paragraph, the amendments made by this section [amending this section] shall take effect as if included in the amendments made by section 803 of the Tax Reform Act of 1986 [section 803 of Pub. L. 99-514].

“(2) SUBSECTION (b).—

“(A) IN GENERAL.—The amendments made by subsection (b) [amending this section] shall apply to costs incurred after December 31, 1988, in taxable years ending after such date.

“(B) REVOCATION OF ELECTION.—If a taxpayer engaged in a farming business involving the production of animals having a preproductive period of more than 2 years made an election under section 263A(d)(3) of the 1986 Code for a taxable year beginning before January 1, 1989, such taxpayer may, without the consent of the Secretary of the Treasury or his delegate, revoke such election effective for the taxpayer’s 1st taxable year beginning after December 31, 1988.”

EFFECTIVE DATE

Section 7831(d)(2) of Pub. L. 101-239 provided that: “If any interest costs incurred after December 31, 1986, are attributable to costs incurred before January 1, 1987, the amendments made by section 803 of the Tax Reform Act of 1986 [section 803 of Pub. L. 99-514, enacting this section, amending sections 48, 267, 312, 447, 464, and 471 of this title, and repealing sections 189, 278, and 280 of this title] shall apply to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954 and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of the Tax Reform Act of 1986) or, if applicable, section 266 of such Code.”

Section 803(d) of Pub. L. 99-514, as amended by Pub. L. 100-647, title I, §1008(b)(7), Nov. 10, 1988, 102 Stat. 3438; Pub. L. 101-239, title VII, §7831(d)(1), Dec. 19, 1989, 103 Stat. 2426, provided that:

“(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [enacting this section, amending sections 48, 267, 312, 447, 464, and 471 of this title, and repealing sections 189, 278, and 280 of this title] shall apply to costs incurred after December 31, 1986, in taxable years ending after such date.

“(2) SPECIAL RULE FOR INVENTORY PROPERTY.—In the case of any property which is inventory in the hands of the taxpayer—

“(A) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1986.

“(B) CHANGE IN METHOD OF ACCOUNTING.—If the taxpayer is required by the amendments made by this section to change its method of accounting with respect to such property for any taxable year—

“(i) such change shall be treated as initiated by the taxpayer,

“(ii) such change shall be treated as made with the consent of the Secretary, and

“(iii) the period for taking into account the adjustments under section 481 by reason of such change shall not exceed 4 years.

“(3) SPECIAL RULE FOR SELF-CONSTRUCTED PROPERTY.—The amendments made by this section shall not apply to any property which is produced by the taxpayer for use by the taxpayer if substantial construction had occurred before March 1, 1986.

“(4) TRANSITIONAL RULE FOR CAPITALIZATION OF INTEREST AND TAXES.—

“(A) TRANSITION PROPERTY EXEMPTED FROM INTEREST CAPITALIZATION.—Section 263A of the Internal

Revenue Code of 1986 (as added by this section) and the amendment made by subsection (b)(1) [repealing section 189 of this title] shall not apply to interest costs which are allocable to any property—

“(i) to which the amendments made by section 201 [amending sections 46, 167, 168, 178, 179, 280F, 291, 312, 465, 467, 514, 751, 1245, 4162, 6111, and 7701 of this title] do not apply by reason of sections 204(a)(1)(D) and (E) and 204(a)(5)(A) [set out as a note under section 168 of this title], and

“(ii) to which the amendments made by section 251 [amending sections 46 and 48 of this title and enacting provisions set out as a note under section 46 of this title] do not apply by reason of section 251(d)(3)(M) [set out as a note under section 46 of this title].

“(B) INTEREST AND TAXES.—Section 263A of such Code shall not apply to property described in the matter following subparagraph (B) of section 207(e)(2) of the Tax Equity and Fiscal Responsibility Act of 1982 [section 207(e)(2)(B) of Pub. L. 97-248, formerly set out as a note under section 189 of this title] to the extent it would require the capitalization of interest and taxes paid or incurred in connection with such property which are not required to be capitalized under section 189 of such Code (as in effect before the amendment made by subsection (b)(1)) [repealing section 189 of this title].

“(5) TRANSITION RULE CONCERNING CAPITALIZATION OF INVENTORY RULES.—In the case of a corporation which on the date of the enactment of this Act [Oct. 22, 1986] was a member of an affiliated group of corporations (within the meaning of section 1504(a) of the Internal Revenue Code of 1986), the parent of which—

“(A) was incorporated in California on April 15, 1925,

“(B) adopted LIFO accounting as of the close of the taxable year ended December 31, 1950, and

“(C) was, on May 22, 1986, merged into a Delaware corporation incorporated on March 12, 1986, the amendments made by this section shall apply under a cut-off method whereby the uniform capitalization rules are applied only in costing layers of inventory acquired during taxable years beginning on or after January 1, 1987.

“(6) TREATMENT OF CERTAIN REHABILITATION PROJECT.—The amendments made by this section shall not apply to interest and taxes paid or incurred with respect to the rehabilitation and conversion of a certified historic building which was formerly a factory into an apartment project with 155 units, 39 units of which are for low-income families, if the project was approved for annual interest assistance on June 10, 1986, by the housing authority of the State in which the project is located.

“(7) SPECIAL RULE FOR CASUALTY LOSSES.—Section 263A(d)(2) of the Internal Revenue Code of 1986 (as added by this section) shall apply to expenses incurred on or after the date of the enactment of this Act [Oct. 22, 1986].”

ALLOCATION RATIO FOR APPORTIONING STORAGE COSTS AND RELATED HANDLING COSTS

Section 1008(b)(8) of Pub. L. 100-647 provided that: “The allocation used in the regulations prescribed under section 263A(h)(2) of the Internal Revenue Code of 1986 for apportioning storage costs and related handling costs shall be determined by dividing the amount of such costs by the beginning inventory balances and the purchases during the year and by multiplying the resulting allocation ratio by inventory amounts determined in accordance with the provisions of the joint explanatory statement of the committee of conference of the conference report accompanying H.R. 3838 (H.R. Rept. No. 99-841, Vol. II., 99th Cong., 2d Sess. II-306-307 (1986)).”

AMORTIZATION OF PAST SERVICE PENSION COSTS

Pub. L. 100-203, title X, § 10204, Dec. 22, 1987, 101 Stat. 1330-394, provided that:

“(a) IN GENERAL.—For purposes of sections 263A and 460 of the Internal Revenue Code of 1986, the allocable costs (within the meaning of section 263A(a)(2) or section 460(c) of such Code, whichever is applicable) with respect to any property shall include contributions paid to or under a pension or annuity plan whether or not such contributions represent past service costs.

“(b) EFFECTIVE DATE.—

“(1) IN GENERAL.—Except as provided in paragraph (2), subsection (a) shall apply to costs incurred after December 31, 1987, in taxable years ending after such date.

“(2) SPECIAL RULE FOR INVENTORY PROPERTY.—In the case of any property which is inventory in the hands of the taxpayer—

“(A) IN GENERAL.—Subsection (a) shall apply to taxable years beginning after December 31, 1987.

“(B) CHANGE IN METHOD OF ACCOUNTING.—If the taxpayer is required by this section to change its method of accounting for any taxable year—

“(i) such change shall be treated as initiated by the taxpayer,

“(ii) such change shall be treated as made with the consent of the Secretary of the Treasury or his delegate, and

“(iii) the net amount of adjustments required by section 481 of the Internal Revenue Code of 1986 shall be taken into account over a period not longer than 4 taxable years.”

§ 264. Certain amounts paid in connection with insurance contracts

(a) General rule

No deduction shall be allowed for—

(1) Premiums on any life insurance policy, or endowment or annuity contract, if the taxpayer is directly or indirectly a beneficiary under the policy or contract.

(2) Any amount paid or accrued on indebtedness incurred or continued to purchase or carry a single premium life insurance, endowment, or annuity contract.

(3) Except as provided in subsection (d), any amount paid or accrued on indebtedness incurred or continued to purchase or carry a life insurance, endowment, or annuity contract (other than a single premium contract or a contract treated as a single premium contract) pursuant to a plan of purchase which contemplates the systematic direct or indirect borrowing of part or all of the increases in the cash value of such contract (either from the insurer or otherwise).

(4) Except as provided in subsection (e), any interest paid or accrued on any indebtedness with respect to 1 or more life insurance policies owned by the taxpayer covering the life of any individual, or any endowment or annuity contracts owned by the taxpayer covering any individual.

Paragraph (2) shall apply in respect of annuity contracts only as to contracts purchased after March 1, 1954. Paragraph (3) shall apply only in respect of contracts purchased after August 6, 1963. Paragraph (4) shall apply with respect to contracts purchased after June 20, 1986.

(b) Exceptions to subsection (a)(1)

Subsection (a)(1) shall not apply to—

(1) any annuity contract described in section 72(s)(5), and

(2) any annuity contract to which section 72(u) applies.

(c) Contracts treated as single premium contracts

For purposes of subsection (a)(2), a contract shall be treated as a single premium contract—

- (1) if substantially all the premiums on the contract are paid within a period of 4 years from the date on which the contract is purchased, or
- (2) if an amount is deposited after March 1, 1954, with the insurer for payment of a substantial number of future premiums on the contract.

(d) Exceptions

Subsection (a)(3) shall not apply to any amount paid or accrued by a person during a taxable year on indebtedness incurred or continued as part of a plan referred to in subsection (a)(3)—

- (1) if no part of 4 of the annual premiums due during the 7-year period (beginning with the date the first premium on the contract to which such plan relates was paid) is paid under such plan by means of indebtedness,
- (2) if the total of the amounts paid or accrued by such person during such taxable year for which (without regard to this paragraph) no deduction would be allowable by reason of subsection (a)(3) does not exceed \$100,
- (3) if such amount was paid or accrued on indebtedness incurred because of an unforeseen substantial loss of income or unforeseen substantial increase in his financial obligations, or
- (4) if such indebtedness was incurred in connection with his trade or business.

For purposes of applying paragraph (1), if there is a substantial increase in the premiums on a contract, a new 7-year period described in such paragraph with respect to such contract shall commence on the date of first such increased premium is paid.

(e) Special rules for application of subsection (a)(4)**(1) Exception for key persons**

Subsection (a)(4) shall not apply to any interest paid or accrued on any indebtedness with respect to policies or contracts covering an individual who is a key person to the extent that the aggregate amount of such indebtedness with respect to policies and contracts covering such individual does not exceed \$50,000.

(2) Interest rate cap on key persons and pre-1986 contracts**(A) In general**

No deduction shall be allowed by reason of paragraph (1) or the last sentence of subsection (a) with respect to interest paid or accrued for any month beginning after December 31, 1995, to the extent the amount of such interest exceeds the amount which would have been determined if the applicable rate of interest were used for such month.

(B) Applicable rate of interest

For purposes of subparagraph (A)—

(i) In general

The applicable rate of interest for any month is the rate of interest described as

Moody's Corporate Bond Yield Average—Monthly Average Corporates as published by Moody's Investors Service, Inc., or any successor thereto, for such month.

(ii) Pre-1986 contracts

In the case of indebtedness on a contract purchased on or before June 30, 1986—

- (I) which is a contract providing a fixed rate of interest, the applicable rate of interest for any month shall be the Moody's rate described in clause (i) for the month in which the contract was purchased, or
- (II) which is a contract providing a variable rate of interest, the applicable rate of interest for any month in an applicable period shall be such Moody's rate for the third month preceding the first month in such period.

For purposes of subclause (II), the term "applicable period" means the 12-month period beginning on the date the policy is issued (and each successive 12-month period thereafter) unless the taxpayer elects a number of months (not greater than 12) other than such 12-month period to be its applicable period. Such an election shall be made not later than the 90th day after the date of the enactment of this sentence and, if made, shall apply to the taxpayer's first taxable year ending on or after October 13, 1995, and all subsequent taxable years unless revoked with the consent of the Secretary.

(3) Key person

For purposes of paragraph (1), the term "key person" means an officer or 20-percent owner, except that the number of individuals who may be treated as key persons with respect to any taxpayer shall not exceed the greater of—

- (A) 5 individuals, or
- (B) the lesser of 5 percent of the total officers and employees of the taxpayer or 20 individuals.

(4) 20-percent owner

For purposes of this subsection, the term "20-percent owner" means—

- (A) if the taxpayer is a corporation, any person who owns directly 20 percent or more of the outstanding stock of the corporation or stock possessing 20 percent or more of the total combined voting power of all stock of the corporation, or
- (B) if the taxpayer is not a corporation, any person who owns 20 percent or more of the capital or profits interest in the taxpayer.

(5) Aggregation rules**(A) In general**

For purposes of paragraph (4)(A) and applying the \$50,000 limitation in paragraph (1)—

- (i) all members of a controlled group shall be treated as one taxpayer, and
- (ii) such limitation shall be allocated among the members of such group in such manner as the Secretary may prescribe.

(B) Controlled group

For purposes of this paragraph, all persons treated as a single employer under subsection (a) or (b) of section 52 or subsection (m) or (o) of section 414 shall be treated as members of a controlled group.

(f) Pro rata allocation of interest expense to policy cash values**(1) In general**

No deduction shall be allowed for that portion of the taxpayer's interest expense which is allocable to unborrowed policy cash values.

(2) Allocation

For purposes of paragraph (1), the portion of the taxpayer's interest expense which is allocable to unborrowed policy cash values is an amount which bears the same ratio to such interest expense as—

(A) the taxpayer's average unborrowed policy cash values of life insurance policies, and annuity and endowment contracts, issued after June 8, 1997, bears to

(B) the sum of—

(i) in the case of assets of the taxpayer which are life insurance policies or annuity or endowment contracts, the average unborrowed policy cash values of such policies and contracts, and

(ii) in the case of assets of the taxpayer not described in clause (i), the average adjusted bases (within the meaning of section 1016) of such assets.

(3) Unborrowed policy cash value

For purposes of this subsection, the term "unborrowed policy cash value" means, with respect to any life insurance policy or annuity or endowment contract, the excess of—

(A) the cash surrender value of such policy or contract determined without regard to any surrender charge, over

(B) the amount of any loan with respect to such policy or contract.

If the amount described in subparagraph (A) with respect to any policy or contract does not reasonably approximate its actual value, the amount taken into account under subparagraph (A) shall be the greater of the amount of the insurance company liability or the insurance company reserve with respect to such policy or contract (as determined for purposes of the annual statement approved by the National Association of Insurance Commissioners) or shall be such other amount as is determined by the Secretary.

(4) Exception for certain policies and contracts**(A) Policies and contracts covering 20-percent owners, officers, directors, and employees**

Paragraph (1) shall not apply to any policy or contract owned by an entity engaged in a trade or business if such policy or contract covers only 1 individual and if such individual is (at the time first covered by the policy or contract)—

- (i) a 20-percent owner of such entity, or
- (ii) an individual (not described in clause (i)) who is an officer, director, or employee of such trade or business.

A policy or contract covering a 20-percent owner of such entity shall not be treated as failing to meet the requirements of the preceding sentence by reason of covering the joint lives of such owner and such owner's spouse.

(B) Contracts subject to current income inclusion

Paragraph (1) shall not apply to any annuity contract to which section 72(u) applies.

(C) Coordination with paragraph (2)

Any policy or contract to which paragraph (1) does not apply by reason of this paragraph shall not be taken into account under paragraph (2).

(D) 20-percent owner

For purposes of subparagraph (A), the term "20-percent owner" has the meaning given such term by subsection (e)(4).

(E) Master contracts

If coverage for each insured under a master contract is treated as a separate contract for purposes of sections 817(h), 7702, and 7702A, coverage for each such insured shall be treated as a separate contract for purposes of subparagraph (A). For purposes of the preceding sentence, the term "master contract" shall not include any group life insurance contract (as defined in section 848(e)(2)).

(5) Exception for policies and contracts held by natural persons; treatment of partnerships and S corporations**(A) Policies and contracts held by natural persons****(i) In general**

This subsection shall not apply to any policy or contract held by a natural person.

(ii) Exception where business is beneficiary

If a trade or business is directly or indirectly the beneficiary under any policy or contract, such policy or contract shall be treated as held by such trade or business and not by a natural person.

(iii) Special rules**(I) Certain trades or businesses not taken into account**

Clause (ii) shall not apply to any trade or business carried on as a sole proprietorship and to any trade or business performing services as an employee.

(II) Limitation on unborrowed cash value

The amount of the unborrowed cash value of any policy or contract which is taken into account by reason of clause (ii) shall not exceed the benefit to which the trade or business is directly or indirectly entitled under the policy or contract.

(iv) Reporting

The Secretary shall require such reporting from policyholders and issuers as is necessary to carry out clause (ii).

(B) Treatment of partnerships and S corporations

In the case of a partnership or S corporation, this subsection shall be applied at the partnership and corporate levels.

(6) Special rules**(A) Coordination with subsection (a) and section 265**

If interest on any indebtedness is disallowed under subsection (a) or section 265—

(i) such disallowed interest shall not be taken into account for purposes of applying this subsection, and

(ii) the amount otherwise taken into account under paragraph (2)(B) shall be reduced (but not below zero) by the amount of such indebtedness.

(B) Coordination with section 263A

This subsection shall be applied before the application of section 263A (relating to capitalization of certain expenses where taxpayer produces property).

(7) Interest expense

The term “interest expense” means the aggregate amount allowable to the taxpayer as a deduction for interest (within the meaning of section 265(b)(4)) for the taxable year (determined without regard to this subsection, section 265(b), and section 291).

(8) Aggregation rules**(A) In general**

All members of a controlled group (within the meaning of subsection (e)(5)(B)) shall be treated as 1 taxpayer for purposes of this subsection.

(B) Treatment of insurance companies

This subsection shall not apply to an insurance company subject to tax under subchapter L, and subparagraph (A) shall be applied without regard to any member of an affiliated group which is an insurance company.

(Aug. 16, 1954, ch. 736, 68A Stat. 77; Pub. L. 88-272, title II, §215(a), (b), Feb. 26, 1964, 78 Stat. 55; Pub. L. 99-514, title X, §1003(a), (b), Oct. 22, 1986, 100 Stat. 2388; Pub. L. 104-191, title V, §501(a), (b), Aug. 21, 1996, 110 Stat. 2090; Pub. L. 105-34, title X, §1084(a), (b)(1), (c), title XVI, §1602(f)(1)–(3), Aug. 5, 1997, 111 Stat. 951, 952, 1094, 1095; Pub. L. 105-206, title VI, §6010(o)(1)–(3)(A), (4)(A), (5), July 22, 1998, 112 Stat. 816; Pub. L. 105-277, div. J, title IV, §4003(i), Oct. 21, 1998, 112 Stat. 2681–910.)

REFERENCES IN TEXT

The date of the enactment of this sentence, referred to in subsection (e)(2)(B)(ii), probably means the date of enactment of Pub. L. 105-34, which was approved Aug. 5, 1997.

CODIFICATION

Another section 1084(b) of Pub. L. 105-34 amended sections 805, 807, 812, and 832 of this title. Another section 1084(c) of Pub. L. 105-34 amended section 265 of this title.

AMENDMENTS

1998—Subsec. (a)(3). Pub. L. 105-206, §6010(o)(1), substituted “subsection (d)” for “subsection (c)”.

Subsec. (a)(4). Pub. L. 105-206, §6010(o)(2), substituted “subsection (e)” for “subsection (d)”.

Subsec. (f)(3). Pub. L. 105-277 inserted concluding provisions.

Subsec. (f)(4)(E). Pub. L. 105-206, §6010(o)(3)(A), added subpar. (E).

Subsec. (f)(5)(A)(iv). Pub. L. 105-206, §6010(o)(4)(A), struck out at end “Any report required under the preceding sentence shall be treated as a statement referred to in section 6724(d)(1).”

Subsec. (f)(8)(A). Pub. L. 105-206, §6010(o)(5), substituted “subsection (e)(5)(B)” for “subsection (d)(5)(B)”.

1997—Subsec. (a)(1). Pub. L. 105-34, §1084(a)(1), amended par. (1) generally. Prior to amendment, par. (1) read as follows: “Premiums paid on any life insurance policy covering the life of any officer or employee, or of any person financially interested in any trade or business carried on by the taxpayer, when the taxpayer is directly or indirectly a beneficiary under such policy.”

Subsec. (a)(4). Pub. L. 105-34, §1602(f)(1), added subpars. (A) and (B) and concluding provisions and struck out former subpars. (A) and (B) and concluding provisions which read as follows:

“(A) is an officer or employee of, or

“(B) is financially interested in,

any trade or business carried on by the taxpayer.”

Pub. L. 105-34, §1084(b)(1), substituted “individual.” for “individual, who—

“(A) is or was an officer or employee, or

“(B) is or was financially interested in,

any trade or business carried on (currently or formerly) by the taxpayer.”

Subsecs. (b), (c). Pub. L. 105-34, §1084(a)(2), added subsec. (b) and redesignated former subsec. (b) as (c). Former subsec. (c) redesignated (d).

Subsec. (d). Pub. L. 105-34, §1084(a)(2), redesignated subsec. (c) as (d). Former subsec. (d) redesignated (e).

Subsec. (d)(2)(B)(ii). Pub. L. 105-34, §1602(f)(2), amended concluding provisions generally. Prior to amendment, concluding provisions read as follows: “For purposes of subclause (II), the taxpayer shall elect an applicable period for such contract on its return of tax imposed by this chapter for its first taxable year ending on or after October 13, 1995. Such applicable period shall be for any number of months (not greater than 12) specified in the election and may not be changed by the taxpayer without the consent of the Secretary.”

Subsec. (d)(4)(B). Pub. L. 105-34, §1602(f)(3), substituted “interest in the taxpayer” for “interest in the employer”.

Subsec. (e). Pub. L. 105-34, §1084(a)(2), redesignated subsec. (d) as (e).

Subsec. (f). Pub. L. 105-34, §1084(c), added subsec. (f).

1996—Subsec. (a)(4). Pub. L. 104-191, §501(a)(1), (b)(1), in introductory provisions, substituted “Except as provided in subsection (d), any” for “Any” and inserted “, or any endowment or annuity contracts owned by the taxpayer covering any individual,” after “the life of any individual”.

Pub. L. 104-191, §501(a)(2), struck out “to the extent that the aggregate amount of such indebtedness with respect to policies covering such individual exceeds \$50,000” after “carried on by the taxpayer” in concluding provisions.

Subsec. (d). Pub. L. 104-191, §501(b)(2), added subsec. (d).

1986—Subsec. (a). Pub. L. 99-514 added par. (4) and last sentence providing that par. (4) shall apply with respect to contracts purchased after June 20, 1986.

1964—Subsec. (a). Pub. L. 88-272 added par. (3) and sentence providing that par. (3) shall apply only to contracts purchased after August 6, 1963.

Subsec. (c). Pub. L. 88-272 added subsec. (c).

EFFECTIVE DATE OF 1998 AMENDMENTS

Amendment by Pub. L. 105-277 effective as if included in the provision of the Taxpayer Relief Act of 1997, Pub. L. 105-34, to which such amendment relates, see section 4003(l) of Pub. L. 105-277, set out as a note under section 86 of this title.

Amendment by Pub. L. 105-206 effective, except as otherwise provided, as if included in the provisions of the Taxpayer Relief Act of 1997, Pub. L. 105-34, to which such amendment relates, see section 6024 of Pub. L. 105-206, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by section 1084(a), (b)(1), (c) of Pub. L. 105-34 applicable to contracts issued after June 8, 1997, in taxable years ending after such date, with special provisions relating to changes in contracts to be treated as new contracts, see section 1084(d) of Pub. L. 105-34, set out as a note under section 101 of this title.

Amendment by section 1602(f)(1)-(3) of Pub. L. 105-34 effective as if included in the provisions of the Health Insurance Portability and Accountability Act of 1996, Pub. L. 104-191, to which such amendment relates, see section 1602(i) of Pub. L. 105-34, set out as a note under section 26 of this title.

EFFECTIVE DATE OF 1996 AMENDMENT

Section 501(c) of Pub. L. 104-191, as amended by Pub. L. 105-34, title XVI, §1602(f)(4), Aug. 5, 1997, 111 Stat. 1095, provided that:

“(1) IN GENERAL.—The amendments made by this section [amending this section] shall apply to interest paid or accrued after October 13, 1995.

“(2) TRANSITION RULE FOR EXISTING INDEBTEDNESS.—

“(A) IN GENERAL.—In the case of—

“(i) indebtedness incurred before January 1, 1996, or

“(ii) indebtedness incurred before January 1, 1997 with respect to any contract or policy entered into in 1994 or 1995,

the amendments made by this section shall not apply to qualified interest paid or accrued on such indebtedness after October 13, 1995, and before January 1, 1999.

“(B) QUALIFIED INTEREST.—For purposes of subparagraph (A), the qualified interest with respect to any indebtedness for any month is the amount of interest (otherwise deductible) which would be paid or accrued for such month on such indebtedness if—

“(i) in the case of any interest paid or accrued after December 31, 1995, indebtedness with respect to no more than 20,000 insured individuals were taken into account, and

“(ii) the lesser of the following rates of interest were used for such month:

“(I) The rate of interest specified under the terms of the indebtedness as in effect on October 13, 1995 (and without regard to modification of such terms after such date).

“(II) The applicable percentage of the rate of interest described as Moody’s Corporate Bond Yield Average-Monthly Average Corporates as published by Moody’s Investors Service, Inc., or any successor thereto, for such month.

For purposes of clause (i), all persons treated as a single employer under subsection (a) or (b) of section 52 of the Internal Revenue Code of 1986 or subsection (m) or (o) of section 414 of such Code shall be treated as 1 person. Subclause (II) of clause (ii) shall not apply to any month before January 1, 1996.

“(C) APPLICABLE PERCENTAGE.—For purposes of subparagraph (B), the applicable percentage is as follows:

For calendar year:	The percentage is:
1996	100 percent
1997	90 percent
1998	80 percent.”

EFFECTIVE DATE OF 1986 AMENDMENT

Section 1003(c) of Pub. L. 99-514 provided that: “The amendments made by this section [amending this section] shall apply to contracts purchased after June 20, 1986, in taxable years ending after such date.”

EFFECTIVE DATE OF 1964 AMENDMENT

Section 215(c) of Pub. L. 88-272 provided that: “The amendments made by this section [amending this sec-

tion] shall apply with respect to amounts paid or accrued in taxable years beginning after December 31, 1963.”

SPREAD OF INCOME INCLUSION ON SURRENDER, ETC. OF CONTRACTS

Section 501(d) of Pub. L. 104-191, as amended by Pub. L. 105-34, title XVI, §1602(f)(5), Aug. 5, 1997, 111 Stat. 1095, provided that:

“(1) IN GENERAL.—If any amount is received under any life insurance policy or endowment or annuity contract described in paragraph (4) of section 264(a) of the Internal Revenue Code of 1986—

“(A) on the complete surrender, redemption, or maturity of such policy or contract during calendar year 1996, 1997, or 1998, or

“(B) in full discharge during any such calendar year of the obligation under the policy or contract which is in the nature of a refund of the consideration paid for the policy or contract,

then (in lieu of any other inclusion in gross income) such amount shall be includible in gross income ratably over the 4-taxable year period beginning with the taxable year such amount would (but for this paragraph) be includible. The preceding sentence shall only apply to the extent the amount is includible in gross income for the taxable year in which the event described in subparagraph (A) or (B) occurs.

“(2) SPECIAL RULES FOR APPLYING SECTION 264.—A contract shall not be treated as—

“(A) failing to meet the requirement of section 264(c)(1) of the Internal Revenue Code of 1986, or

“(B) a single premium contract under section 264(b)(1) of such Code,

solely by reason of an occurrence described in subparagraph (A) or (B) of paragraph (1) of this subsection or solely by reason of a lapse occurring after October 13, 1995, by reason of no additional premiums being received under the contract.

“(3) SPECIAL RULE FOR DEFERRED ACQUISITION COSTS.—In the case of the occurrence of any event described in subparagraph (A) or (B) of paragraph (1) of this subsection with respect to any policy or contract—

“(A) section 848 of the Internal Revenue Code of 1986 shall not apply to the unamortized balance (if any) of the specified policy acquisition expenses attributable to such policy or contract immediately before the insurance company’s taxable year in which such event occurs, and

“(B) there shall be allowed as a deduction to such company for such taxable year under chapter 1 of such Code an amount equal to such unamortized balance.”

§ 265. Expenses and interest relating to tax-exempt income

(a) General rule

No deduction shall be allowed for—

(1) Expenses

Any amount otherwise allowable as a deduction which is allocable to one or more classes of income other than interest (whether or not any amount of income of that class or classes is received or accrued) wholly exempt from the taxes imposed by this subtitle, or any amount otherwise allowable under section 212 (relating to expenses for production of income) which is allocable to interest (whether or not any amount of such interest is received or accrued) wholly exempt from the taxes imposed by this subtitle.

(2) Interest

Interest on indebtedness incurred or continued to purchase or carry obligations the interest on which is wholly exempt from the taxes imposed by this subtitle.

(3) Certain regulated investment companies

In the case of a regulated investment company which distributes during the taxable year an exempt-interest dividend (including exempt-interest dividends paid after the close of the taxable year as described in section 855), that portion of any amount otherwise allowable as a deduction which the amount of the income of such company wholly exempt from taxes under this subtitle bears to the total of such exempt income and its gross income (excluding from gross income, for this purpose, capital gain net income, as defined in section 1222(9)).

(4) Interest related to exempt-interest dividends

Interest on indebtedness incurred or continued to purchase or carry shares of stock of a regulated investment company which during the taxable year of the holder thereof distributes exempt-interest dividends.

(5) Special rules for application of paragraph (2) in the case of short sales

For purposes of paragraph (2)—

(A) In general

The term “interest” includes any amount paid or incurred—

- (i) by any person making a short sale in connection with personal property used in such short sale, or
- (ii) by any other person for the use of any collateral with respect to such short sale.

(B) Exception where no return on cash collateral

If—

- (i) the taxpayer provides cash as collateral for any short sale, and
- (ii) the taxpayer receives no material earnings on such cash during the period of the sale,

subparagraph (A)(i) shall not apply to such short sale.

(6) Section not to apply with respect to parsonage and military housing allowances

No deduction shall be denied under this section for interest on a mortgage on, or real property taxes on, the home of the taxpayer by reason of the receipt of an amount as—

- (A) a military housing allowance, or
- (B) a parsonage allowance excludable from gross income under section 107.

(b) Pro rata allocation of interest expense of financial institutions to tax-exempt interest**(1) In general**

In the case of a financial institution, no deduction shall be allowed for that portion of the taxpayer's interest expense which is allocable to tax-exempt interest.

(2) Allocation

For purposes of paragraph (1), the portion of the taxpayer's interest expense which is allocable to tax-exempt interest is an amount which bears the same ratio to such interest expense as—

(A) the taxpayer's average adjusted bases (within the meaning of section 1016) of tax-exempt obligations acquired after August 7, 1986, bears to

(B) such average adjusted bases for all assets of the taxpayer.

(3) Exception for certain tax-exempt obligations**(A) In general**

Any qualified tax-exempt obligation acquired after August 7, 1986, shall be treated for purposes of paragraph (2) and section 291(e)(1)(B) as if it were acquired on August 7, 1986.

(B) Qualified tax-exempt obligation**(i) In general**

For purposes of subparagraph (A), the term “qualified tax-exempt obligation” means a tax-exempt obligation—

- (I) which is issued after August 7, 1986, by a qualified small issuer,
- (II) which is not a private activity bond (as defined in section 141), and
- (III) which is designated by the issuer for purposes of this paragraph.

(ii) Certain bonds not treated as private activity bonds

For purposes of clause (i)(II), there shall not be treated as a private activity bond—

- (I) any qualified 501(c)(3) bond (as defined in section 145), or
- (II) any obligation issued to refund (or which is part of a series of obligations issued to refund) an obligation issued before August 8, 1986, which was not an industrial development bond (as defined in section 103(b)(2) as in effect on the day before the date of the enactment of the Tax Reform Act of 1986) or a private loan bond (as defined in section 103(o)(2)(A), as so in effect, but without regard to any exemption from such definition other than section 103(o)(2)(A)).

(C) Qualified small issuer**(i) In general**

For purposes of subparagraph (B), the term “qualified small issuer” means, with respect to obligations issued during any calendar year, any issuer if the reasonably anticipated amount of tax-exempt obligations (other than obligations described in clause (ii)) which will be issued by such issuer during such calendar year does not exceed \$10,000,000.

(ii) Obligations not taken into account in determining status as qualified small issuer

For purposes of clause (i), an obligation is described in this clause if such obligation is—

- (I) a private activity bond (other than a qualified 501(c)(3) bond, as defined in section 145),
- (II) an obligation to which section 141(a) does not apply by reason of section 1312, 1313, 1316(g), or 1317 of the Tax Reform Act of 1986 and which would (if is—

sued on August 15, 1986) have been an industrial development bond (as defined in section 103(b)(2) as in effect on the day before the date of the enactment of such Act) or a private loan bond (as defined in section 103(o)(2)(A), as so in effect, but without regard to any exception from such definition other than section 103(o)(2)(A)), or

(III) an obligation issued to refund (other than to advance refund within the meaning of section 149(d)(5)) any obligation to the extent the amount of the refunding obligation does not exceed the outstanding amount of the refunded obligation.

(iii) Allocation of amount of issue in certain cases

In the case of an issue under which more than 1 governmental entity receives benefits, if—

(I) all governmental entities receiving benefits from such issue irrevocably agree (before the date of issuance of the issue) on an allocation of the amount of such issue for purposes of this subparagraph, and

(II) such allocation bears a reasonable relationship to the respective benefits received by such entities,

then the amount of such issue so allocated to an entity (and only such amount with respect to such issue) shall be taken into account under clause (i) with respect to such entity.

(D) Limitation on amount of obligations which may be designated

(i) In general

Not more than \$10,000,000 of obligations issued by an issuer during any calendar year may be designated by such issuer for purposes of this paragraph.

(ii) Certain refundings of designated obligations deemed designated

Except as provided in clause (iii), in the case of a refunding (or series of refundings) of a qualified tax-exempt obligation, the refunding obligation shall be treated as a qualified tax-exempt obligation (and shall not be taken into account under clause (i)) if—

(I) the refunding obligation was not taken into account under subparagraph (C) by reason of clause (ii)(III) thereof,

(II) the average maturity date of the refunding obligations issued as part of the issue of which such refunding obligation is a part is not later than the average maturity date of the obligations to be refunded by such issue, and

(III) the refunding obligation has a maturity date which is not later than the date which is 30 years after the date the original qualified tax-exempt obligation was issued.

Subclause (II) shall not apply if the average maturity of the issue of which the original qualified tax-exempt obligation

was a part (and of the issue of which the obligations to be refunded are a part) is 3 years or less. For purposes of this clause, average maturity shall be determined in accordance with section 147(b)(2)(A).

(iii) Certain obligations may not be designated or deemed designated

No obligation issued as part of an issue may be designated under this paragraph (or may be treated as designated under clause (ii)) if—

(I) any obligation issued as part of such issue is issued to refund another obligation, and

(II) the aggregate face amount of such issue exceeds \$10,000,000.

(E) Aggregation of issuers

For purposes of subparagraphs (C) and (D)—

(i) an issuer and all entities which issue obligations on behalf of such issuer shall be treated as 1 issuer,

(ii) all obligations issued by a subordinate entity shall, for purposes of applying subparagraphs (C) and (D) to each other entity to which such entity is subordinate, be treated as issued by such other entity, and

(iii) an entity formed (or, to the extent provided by the Secretary, availed of) to avoid the purposes of subparagraph (C) or (D) and all entities benefiting thereby shall be treated as 1 issuer.

(F) Treatment of composite issues

In the case of an obligation which is issued as part of a direct or indirect composite issue, such obligation shall not be treated as a qualified tax-exempt obligation unless—

(i) the requirements of this paragraph are met with respect to such composite issue (determined by treating such composite issue as a single issue), and

(ii) the requirements of this paragraph are met with respect to each separate lot of obligations which are part of the issue (determined by treating each such separate lot as a separate issue).

(G) Special rules for obligations issued during 2009 and 2010

(i) Increase in limitation

In the case of obligations issued during 2009 or 2010, subparagraphs (C)(i), (D)(i), and (D)(iii)(II) shall each be applied by substituting “\$30,000,000” for “\$10,000,000”.

(ii) Qualified 501(c)(3) bonds treated as issued by exempt organization

In the case of a qualified 501(c)(3) bond (as defined in section 145) issued during 2009 or 2010, this paragraph shall be applied by treating the 501(c)(3) organization for whose benefit such bond was issued as the issuer.

(iii) Special rule for qualified financings

In the case of a qualified financing issue issued during 2009 or 2010—

(I) subparagraph (F) shall not apply, and

(II) any obligation issued as a part of such issue shall be treated as a qualified tax-exempt obligation if the requirements of this paragraph are met with respect to each qualified portion of the issue (determined by treating each qualified portion as a separate issue which is issued by the qualified borrower with respect to which such portion relates).

(iv) Qualified financing issue

For purposes of this subparagraph, the term “qualified financing issue” means any composite, pooled, or other conduit financing issue the proceeds of which are used directly or indirectly to make or finance loans to 1 or more ultimate borrowers each of whom is a qualified borrower.

(v) Qualified portion

For purposes of this subparagraph, the term “qualified portion” means that portion of the proceeds which are used with respect to each qualified borrower under the issue.

(vi) Qualified borrower

For purposes of this subparagraph, the term “qualified borrower” means a borrower which is a State or political subdivision thereof or an organization described in section 501(c)(3) and exempt from taxation under section 501(a).

(4) Definitions

For purposes of this subsection—

(A) Interest expense

The term “interest expense” means the aggregate amount allowable to the taxpayer as a deduction for interest for the taxable year (determined without regard to this subsection, section 264, and section 291). For purposes of the preceding sentence, the term “interest” includes amounts (whether or not designated as interest) paid in respect of deposits, investment certificates, or withdrawable or repurchasable shares.

(B) Tax-exempt obligation

The term “tax-exempt obligation” means any obligation the interest on which is wholly exempt from taxes imposed by this subtitle. Such term includes shares of stock of a regulated investment company which during the taxable year of the holder thereof distributes exempt-interest dividends.

(5) Financial institution

For purposes of this subsection, the term “financial institution” means any person who—

(A) accepts deposits from the public in the ordinary course of such person’s trade or business, and is subject to Federal or State supervision as a financial institution, or

(B) is a corporation described in section 585(a)(2).

(6) Special rules

(A) Coordination with subsection (a)

If interest on any indebtedness is disallowed under subsection (a) with respect to any tax-exempt obligation—

(i) such disallowed interest shall not be taken into account for purposes of applying this subsection, and

(ii) for purposes of applying paragraph (2), the adjusted basis of such tax-exempt obligation shall be reduced (but not below zero) by the amount of such indebtedness.

(B) Coordination with section 263A

This section shall be applied before the application of section 263A (relating to capitalization of certain expenses where taxpayer produces property).

(7) De minimis exception for bonds issued during 2009 or 2010

(A) In general

In applying paragraph (2)(A), there shall not be taken into account tax-exempt obligations issued during 2009 or 2010.

(B) Limitation

The amount of tax-exempt obligations not taken into account by reason of subparagraph (A) shall not exceed 2 percent of the amount determined under paragraph (2)(B).

(C) Refundings

For purposes of this paragraph, a refunding bond (whether a current or advance refunding) shall be treated as issued on the date of the issuance of the refunded bond (or in the case of a series of refundings, the original bond).

(Aug. 16, 1954, ch. 736, 68A Stat. 78; Pub. L. 88-272, title II, §216(a), Feb. 26, 1964, 78 Stat. 56; Pub. L. 94-455, title XIX, §§1901(a)(37), 1906(b)(13)(A), title XXI, §2137(e), Oct. 4, 1976, 90 Stat. 1770, 1834, 1931; Pub. L. 96-223, title IV, §404(b)(2), Apr. 2, 1980, 94 Stat. 306; Pub. L. 97-34, title III, §§301(b)(2), 302(c)(2), (d)(1), Aug. 13, 1981, 95 Stat. 270, 272, 274; Pub. L. 98-369, div. A, title I, §§16(a), 56(c), July 18, 1984, 98 Stat. 505, 574; Pub. L. 99-514, title I, §144, title IX, §902(a), (b), (d), Oct. 22, 1986, 100 Stat. 2121, 2380-2382; Pub. L. 100-647, title I, §1009(b)(3)(A), Nov. 10, 1988, 102 Stat. 3446; Pub. L. 101-508, title XI, §11801(c)(4), Nov. 5, 1990, 104 Stat. 1388-523; Pub. L. 105-34, title X, §1084(c), Aug. 5, 1997, 111 Stat. 955; Pub. L. 111-5, div. B, title I, §§1501(a), 1502(a), Feb. 17, 2009, 123 Stat. 353.)

REFERENCES IN TEXT

The date of the enactment of the Tax Reform Act of 1986, referred to in subsec. (b)(3)(B)(ii)(II), (C)(ii)(II), is the date of enactment of Pub. L. 99-514, which was approved Oct. 22, 1986.

Sections 1312, 1313, 1316(g), and 1317 of the Tax Reform Act of 1986, referred to in subsec. (b)(3)(C)(ii)(II), are sections 1312, 1313, 1316(g), and 1317 of Pub. L. 99-514, which are set out as a note under section 141 of this title.

CODIFICATION

Another section 1084(c) of Pub. L. 105-34 amended section 264 of this title.

AMENDMENTS

2009—Subsec. (b)(3)(G). Pub. L. 111-5, §1502(a), added subpar. (G).

Subsec. (b)(7). Pub. L. 111-5, §1501(a), added par. (7).

1997—Subsec. (b)(4)(A). Pub. L. 105-34 inserted “, section 264,” before “and section 291”.

1990—Subsec. (a)(2). Pub. L. 101-508, §11801(c)(4), struck out before period at end “, or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128”.

1988—Subsec. (b)(3). Pub. L. 100-647 amended par. (3) generally, reenacting subpar. (A) without change, revising and restating provisions of subpars. (B) to (E), and adding subpar. (F).

1986—Pub. L. 99-514, §902(a), (d), designated existing provisions as subsec. (a), inserted heading, and added subsec. (b).

Par. (2). Pub. L. 99-514, §902(b), struck out last sentence which read as follows: “In applying the preceding sentence to a financial institution (other than a bank) which is a face-amount certificate company registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1 and following) and which is subject to the banking laws of the State in which such institution is incorporated, interest on face-amount certificates (as defined in section 2(a)(15) of such Act) issued by such institution, and interest on amounts received for the purchase of such certificates to be issued by such institution, shall not be considered as interest on indebtedness incurred or continued to purchase or carry obligations the interest on which is wholly exempt from the taxes imposed by this subtitle, to the extent that the average amount of such obligations held by such institution during the taxable year (as determined under regulations prescribed by the Secretary) does not exceed 15 percent of the average of the total assets held by such institution during the taxable year (as so determined).”

Par. (6). Pub. L. 99-514, §144, added par. (6).

1984—Par. (2). Pub. L. 98-369, §16(a), repealed amendments made by Pub. L. 97-34, §302(c). See 1981 Amendment note below.

Par. (5). Pub. L. 98-369, §56(c), added par. (5).

1981—Par. (2). Pub. L. 97-34, §302(c)(2), (d)(1), provided that, applicable to taxable years beginning after Dec. 31, 1984, par. (2) is amended by striking out “or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128” and inserting in lieu thereof “or to purchase or carry obligations or shares, or to make other deposits or investments, the interest on which is described in section 128(c)(1) to the extent such interest is excludable from gross income under section 128”. Section 16(a) of Pub. L. 98-369, repealed section 302(c) of Pub. L. 97-34, and provided that this title shall be applied and administered as if section 302(c), and the amendments made by such section 302(c), had not been enacted.

Pub. L. 97-34, §301(b)(2), inserted “, or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128” after “116”.

1980—Par. (2). Pub. L. 96-223 inserted “, or to purchase or carry obligations or shares, or to make deposits or other investments, the interest on which is described in section 116(c) to the extent such interest is excludable from gross income under section 116” after “subtitle”.

1976—Par. (2). Pub. L. 94-455, §§1901(a)(37), 1906(b)(13)(A), struck out “(other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer)” after “to purchase or carry obligations” and “or his delegate” after “Secretary”.

Pars. (3), (4). Pub. L. 94-455, §2137(e), added pars. (3) and (4).

1964—Par. (2). Pub. L. 88-272 provided that interest on face-amount certificates issued by a face-amount certificate company, and interest on amounts received for the purchase of such certificates to be issued by such institution, shall not be considered interest on indebtedness to purchase or carry obligations the interest on which is wholly exempt from the taxes under this subtitle, to the extent the average amount of such obligations held by such institution during the taxable year doesn't exceed 15 percent of the average total assets held by such institution during the taxable year.

EFFECTIVE DATE OF 2009 AMENDMENT

Pub. L. 111-5, div. B, title I, §1501(c), Feb. 17, 2009, 123 Stat. 353, provided that: “The amendments made by this section [amending this section and section 291 of this title] shall apply to obligations issued after December 31, 2008.”

Pub. L. 111-5, div. B, title I, §1502(b), Feb. 17, 2009, 123 Stat. 354, provided that: “The amendment made by this section [amending this section] shall apply to obligations issued after December 31, 2008.”

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by Pub. L. 105-34 applicable to contracts issued after June 8, 1997, in taxable years ending after such date, with special provisions relating to changes in contracts to be treated as new contracts, see section 1084(d) of Pub. L. 105-34, set out as a note under section 101 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Section 1009(b)(3)(B)–(D) of Pub. L. 100-647, as amended by Pub. L. 101-239, title VII, §7811(f)(2), Dec. 19, 1989, 103 Stat. 2409, provided that:

“(B) In the case of any obligation issued after August 7, 1986, and before January 1, 1987, the time for making a designation with respect to such obligation under section 265(b)(3)(B)(i)(III) of the 1986 Code shall not expire before January 1, 1989.

“(C) If—

“(i) an obligation is issued on or after January 1, 1986, and on or before August 7, 1986,

“(ii) when such obligation was issued, the issuer made a designation that it intended to qualify under section 802(e)(3) of H.R. 3838 of the 99th Congress as passed by the House of Representatives [H.R. 3838 was enacted as Pub. L. 99-514], and

“(iii) the issuer makes an election under this subparagraph with respect to such obligation,

“(D)(i) Except as provided in clause (ii), the following provisions of section 265(b)(3) of the 1986 Code (as amended by this subparagraph (A)) shall apply to obligations issued after June 30, 1987:

“(I) subparagraph (C)(ii)(III),

“(II) clauses (ii) and (iii) of subparagraph (D), and

“(III) subparagraphs (E) and (F).

“(ii) At the election of an issuer (made at such time and in such manner as the Secretary of the Treasury or his delegate may prescribe), the provisions referred to in clause (i) shall apply to such issuer as if included in the amendments made by section 902(a) of the Tax Reform Act of 1986 [section 902(a) of Pub. L. 99-514, amending this section].”

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 144 of Pub. L. 99-514 applicable to taxable years beginning before, on, or after Dec. 31, 1986, see section 151(e) of Pub. L. 99-514, set out as a note under section 1 of this title.

Section 902(f) of Pub. L. 99-514, as amended by Pub. L. 100-647, title I, §1009(b)(1), (2), (7), Nov. 10, 1988, 102 Stat. 3445, 3446, 3449, provided that:

“(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [amending this section and sections 163, 291, and 1277 of this title] shall apply to taxable years ending after December 31, 1986.

“(2) OBLIGATIONS ACQUIRED PURSUANT TO CERTAIN COMMITMENTS.—For purposes of sections 265(b) and 291(e)(1)(B) of the Internal Revenue Code of 1986, any tax-exempt obligation which is acquired after August 7, 1986, pursuant to a direct or indirect written commitment—

“(A) to purchase or repurchase such obligation, and
“(B) entered into on or before September 25, 1985,
shall be treated as an obligation acquired before August 8, 1986.

“(3) TRANSITIONAL RULES.—For purposes of sections 265(b) and 291(e)(1)(B) of the Internal Revenue Code of 1986, obligations with respect to any of the following projects shall be treated as obligations acquired before August 8, 1986, in the hands of the first and any subsequent financial institution acquiring such obligations:

- “(A) Park Forest, Illinois, redevelopment project.
- “(B) Clinton, Tennessee, Carriage Trace project.
- “(C) Savannah, Georgia, Mall Terrace Warehouse project.
- “(D) Chattanooga, Tennessee, Warehouse Row project.
- “(E) Dalton, Georgia, Towne Square project.
- “(F) Milwaukee, Wisconsin, Standard Electric Supply Company—distribution facility.
- “(G) Wausau, Wisconsin, urban renewal project.
- “(H) Cassville, Missouri, UDAG project.
- “(I) Outlook Envelope Company—plant expansion.
- “(J) Woodstock, Connecticut, Crabtree Warehouse partnership.
- “(K) Louisville, Kentucky, Speed Mansion renovation project.
- “(L) Charleston, South Carolina, 2 Festival Market Place projects at Union Pier Terminal and 1 project at the Remount Road Container Yard, State Pier No. 15 at North Charleston Terminal.
- “(M) New Orleans, Louisiana, Upper Pontalba Building renovation.
- “(N) Woodward Wight Building.
- “(O) Minneapolis, Minnesota, Miller Milling Company—flour mill project.
- “(P) Homewood, Alabama, the Club Apartments.
- “(Q) Charlotte, North Carolina—qualified mortgage bonds acquired by NCNB bank (\$5,250,000).
- “(R) Grand Rapids, Michigan, Central Bank project.
- “(S) Ruppman Marketing Services, Inc.—building project.
- “(T) Bellows Falls, Vermont—building project.
- “(U) East Broadway Project, Louisville, Kentucky.
- “(V) O.K. Industries, Oklahoma.

“(4) ADDITIONAL TRANSITIONAL RULE.—Obligations issued pursuant to an allocation of a State’s volume limitation for private activity bonds, which allocation was made by Executive Order 25 signed by the Governor of the State on May 22, 1986 (as such order may be amended before January 1, 1987), and qualified 501(c)(3) bonds designated by such Governor for purposes of this paragraph, shall be treated as acquired on or before August 7, 1986, in the hands of the first and any subsequent financial institution acquiring such obligation. The aggregate face amount of obligations to which this paragraph applies shall not exceed \$200,000,000.”

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 16(a) of Pub. L. 98-369 applicable to taxable years ending after Dec. 31, 1983, see section 18(a) of Pub. L. 98-369, set out as a note under section 48 of this title.

Amendment by section 56(c) of Pub. L. 98-369 applicable to short sales after July 18, 1984, in taxable years ending after that date, see section 56(d) of Pub. L. 98-369, set out as a note under section 163 of this title.

EFFECTIVE DATE OF 1981 AMENDMENT

Section 301(d) of Pub. L. 97-34 provided that:

“(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [enacting section 128 of this title and amending this section and sections 584, 643, and 702 of this title] shall apply to taxable years ending after September 30, 1981.

“(2) CONFORMING AMENDMENTS.—The amendments made by subsection (b)(6) [amending sections 584, 643, and 702 of this title] shall apply to taxable years beginning after December 31, 1981.”

EFFECTIVE AND TERMINATION DATES OF 1980 AMENDMENT

Section 404(c) of Pub. L. 96-223, as amended by Pub. L. 97-34, title III, §302(b)(1), Aug. 13, 1981, 95 Stat. 272,

provided that: “The amendments made by this section [amending this section and sections 116, 584, 643, 702, 854, and 857 of this title] shall apply with respect to taxable years beginning after December 31, 1980, and before January 1, 1982.”

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(a)(37) of Pub. L. 94-455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94-455, set out as a note under section 2 of this title.

Amendment by section 2137(e) of Pub. L. 94-455 effective for taxable years beginning after Dec. 31, 1975, see section 2137(e) of Pub. L. 94-455, set out as a note under section 852 of this title.

EFFECTIVE DATE OF 1964 AMENDMENT

Section 216(b) of Pub. L. 88-272 provided that: “The amendment made by subsection (a) [amending this section] shall apply with respect to taxable years ending after the date of the enactment of this Act [Feb. 21, 1964].”

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101-508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101-508, set out as a note under section 45K of this title.

CLARIFICATION OF TREATMENT OF AMOUNTS EXCLUDED UNDER SECTION 597

Section 904(c)(2)(B) of Pub. L. 99-514 provided that this section shall not deny any deduction by reason of such deduction being allocable to amounts excluded from gross income under section 597 of this title as in effect on Oct. 21, 1986, prior to repeal by Pub. L. 101-73, title XIV, §1401(a)(3)(B), Aug. 9, 1989, 103 Stat. 549.

§ 266. Carrying charges

No deduction shall be allowed for amounts paid or accrued for such taxes and carrying charges as, under regulations prescribed by the Secretary, are chargeable to capital account with respect to property, if the taxpayer elects, in accordance with such regulations, to treat such taxes or charges as so chargeable.

(Aug. 16, 1954, ch. 736, 68A Stat. 78; Pub. L. 94-455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834.)

AMENDMENTS

1976—Pub. L. 94-455 struck out “or his delegate” after “Secretary”.

§ 267. Losses, expenses, and interest with respect to transactions between related taxpayers

(a) In general

(1) Deduction for losses disallowed

No deduction shall be allowed in respect of any loss from the sale or exchange of property, directly or indirectly, between persons specified in any of the paragraphs of subsection (b). The preceding sentence shall not apply to any loss of the distributing corporation (or the distributee) in the case of a distribution in complete liquidation.

(2) Matching of deduction and payee income item in the case of expenses and interest

If—

(A) by reason of the method of accounting of the person to whom the payment is to be made, the amount thereof is not (unless paid) includible in the gross income of such person, and

(B) at the close of the taxable year of the taxpayer for which (but for this paragraph) the amount would be deductible under this chapter, both the taxpayer and the person to whom the payment is to be made are persons specified in any of the paragraphs of subsection (b),

then any deduction allowable under this chapter in respect of such amount shall be allowable as of the day as of which such amount is includible in the gross income of the person to whom the payment is made (or, if later, as of the day on which it would be so allowable but for this paragraph). For purposes of this paragraph, in the case of a personal service corporation (within the meaning of section 441(i)(2)), such corporation and any employee-owner (within the meaning of section 269A(b)(2), as modified by section 441(i)(2)) shall be treated as persons specified in subsection (b).

(3) Payments to foreign persons

(A) In general

The Secretary shall by regulations apply the matching principle of paragraph (2) in cases in which the person to whom the payment is to be made is not a United States person.

(B) Special rule for certain foreign entities

(i) In general

Notwithstanding subparagraph (A), in the case of any item payable to a controlled foreign corporation (as defined in section 957) or a passive foreign investment company (as defined in section 1297), a deduction shall be allowable to the payor with respect to such amount for any taxable year before the taxable year in which paid only to the extent that an amount attributable to such item is includible (determined without regard to properly allocable deductions and qualified deficits under section 952(c)(1)(B)) during such prior taxable year in the gross income of a United States person who owns (within the meaning of section 958(a)) stock in such corporation.

(ii) Secretarial authority

The Secretary may by regulation exempt transactions from the application of clause (i), including any transaction which is entered into by a payor in the ordinary course of a trade or business in which the payor is predominantly engaged and in which the payment of the accrued amounts occurs within 8½ months after accrual or within such other period as the Secretary may prescribe.

(b) Relationships

The persons referred to in subsection (a) are:

(1) Members of a family, as defined in subsection (c)(4);

(2) An individual and a corporation more than 50 percent in value of the outstanding stock of which is owned, directly or indirectly, by or for such individual;

(3) Two corporations which are members of the same controlled group (as defined in subsection (f));

(4) A grantor and a fiduciary of any trust;

(5) A fiduciary of a trust and a fiduciary of another trust, if the same person is a grantor of both trusts;

(6) A fiduciary of a trust and a beneficiary of such trust;

(7) A fiduciary of a trust and a beneficiary of another trust, if the same person is a grantor of both trusts;

(8) A fiduciary of a trust and a corporation more than 50 percent in value of the outstanding stock of which is owned, directly or indirectly, by or for the trust or by or for a person who is a grantor of the trust;

(9) A person and an organization to which section 501 (relating to certain educational and charitable organizations which are exempt from tax) applies and which is controlled directly or indirectly by such person or (if such person is an individual) by members of the family of such individual;

(10) A corporation and a partnership if the same persons own—

(A) more than 50 percent in value of the outstanding stock of the corporation, and

(B) more than 50 percent of the capital interest, or the profits interest, in the partnership;

(11) An S corporation and another S corporation if the same persons own more than 50 percent in value of the outstanding stock of each corporation;

(12) An S corporation and a C corporation, if the same persons own more than 50 percent in value of the outstanding stock of each corporation; or

(13) Except in the case of a sale or exchange in satisfaction of a pecuniary bequest, an executor of an estate and a beneficiary of such estate.

(c) Constructive ownership of stock

For purposes of determining, in applying subsection (b), the ownership of stock—

(1) Stock owned, directly or indirectly, by or for a corporation, partnership, estate, or trust shall be considered as being owned proportionately by or for its shareholders, partners, or beneficiaries;

(2) An individual shall be considered as owning the stock owned, directly or indirectly, by or for his family;

(3) An individual owning (otherwise than by the application of paragraph (2)) any stock in a corporation shall be considered as owning the stock owned, directly or indirectly, by or for his partner;

(4) The family of an individual shall include only his brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants; and

(5) Stock constructively owned by a person by reason of the application of paragraph (1) shall, for the purpose of applying paragraph

(1), (2), or (3), be treated as actually owned by such person, but stock constructively owned by an individual by reason of the application of paragraph (2) or (3) shall not be treated as owned by him for the purpose of again applying either of such paragraphs in order to make another the constructive owner of such stock.

(d) Amount of gain where loss previously disallowed

If—

(1) in the case of a sale or exchange of property to the taxpayer a loss sustained by the transferor is not allowable to the transferor as a deduction by reason of subsection (a)(1) (or by reason of section 24(b) of the Internal Revenue Code of 1939); and

(2) after December 31, 1953, the taxpayer sells or otherwise disposes of such property (or of other property the basis of which in his hands is determined directly or indirectly by reference to such property) at a gain,

then such gain shall be recognized only to the extent that it exceeds so much of such loss as is properly allocable to the property sold or otherwise disposed of by the taxpayer. This subsection applies with respect to taxable years ending after December 31, 1953. This subsection shall not apply if the loss sustained by the transferor is not allowable to the transferor as a deduction by reason of section 1091 (relating to wash sales) or by reason of section 118 of the Internal Revenue Code of 1939.

(e) Special rules for pass-thru entities

(1) In general

In the case of any amount paid or incurred by, to, or on behalf of, a pass-thru entity, for purposes of applying subsection (a)(2)—

(A) such entity,

(B) in the case of—

(i) a partnership, any person who owns (directly or indirectly) any capital interest or profits interest of such partnership, or

(ii) an S corporation, any person who owns (directly or indirectly) any of the stock of such corporation,

(C) any person who owns (directly or indirectly) any capital interest or profits interest of a partnership in which such entity owns (directly or indirectly) any capital interest or profits interest, and

(D) any person related (within the meaning of subsection (b) of this section or section 707(b)(1)) to a person described in subparagraph (B) or (C),

shall be treated as persons specified in a paragraph of subsection (b). Subparagraph (C) shall apply to a transaction only if such transaction is related either to the operations of the partnership described in such subparagraph or to an interest in such partnership.

(2) Pass-thru entity

For purposes of this section, the term “pass-thru entity” means—

(A) a partnership, and

(B) an S corporation.

(3) Constructive ownership in the case of partnerships

For purposes of determining ownership of a capital interest or profits interest of a part-

nership, the principles of subsection (c) shall apply, except that—

(A) paragraph (3) of subsection (c) shall not apply, and

(B) interests owned (directly or indirectly) by or for a C corporation shall be considered as owned by or for any shareholder only if such shareholder owns (directly or indirectly) 5 percent or more in value of the stock of such corporation.

(4) Subsection (a)(2) not to apply to certain guaranteed payments of partnerships

In the case of any amount paid or incurred by a partnership, subsection (a)(2) shall not apply to the extent that section 707(c) applies to such amount.

(5) Exception for certain expenses and interest of partnerships owning low-income housing

(A) In general

This subsection shall not apply with respect to qualified expenses and interest paid or incurred by a partnership owning low-income housing to—

(i) any qualified 5-percent or less partner of such partnership, or

(ii) any person related (within the meaning of subsection (b) of this section or section 707(b)(1)) to any qualified 5-percent or less partner of such partnership.

(B) Qualified 5-percent or less partner

For purposes of this paragraph, the term “qualified 5-percent or less partner” means any partner who has (directly or indirectly) an interest of 5 percent or less in the aggregate capital and profits interests of the partnership but only if—

(i) such partner owned the low-income housing at all times during the 2-year period ending on the date such housing was transferred to the partnership, or

(ii) such partnership acquired the low-income housing pursuant to a purchase, assignment, or other transfer from the Department of Housing and Urban Development or any State or local housing authority.

For purposes of the preceding sentence, a partner shall be treated as holding any interest in the partnership which is held (directly or indirectly) by any person related (within the meaning of subsection (b) of this section or section 707(b)(1)) to such partner.

(C) Qualified expenses and interest

For purpose of this paragraph, the term “qualified expenses and interest” means any expense or interest incurred by the partnership with respect to low-income housing held by the partnership but—

(i) only if the amount of such expense or interest (as the case may be) is unconditionally required to be paid by the partnership not later than 10 years after the date such amount was incurred, and

(ii) in the case of such interest, only if such interest is incurred at an annual rate not in excess of 12 percent.

(D) Low-income housing

For purposes of this paragraph, the term “low-income housing” means—

(i) any interest in property described in clause (i), (ii), (iii), or (iv) of section 1250(a)(1)(B), and

(ii) any interest in a partnership owning such property.

(6) Cross reference

For additional rules relating to partnerships, see section 707(b).

(f) Controlled group defined; special rules applicable to controlled groups**(1) Controlled group defined**

For purposes of this section, the term “controlled group” has the meaning given to such term by section 1563(a), except that—

(A) “more than 50 percent” shall be substituted for “at least 80 percent” each place it appears in section 1563(a), and

(B) the determination shall be made without regard to subsections (a)(4) and (e)(3)(C) of section 1563.

(2) Deferral (rather than denial) of loss from sale or exchange between members

In the case of any loss from the sale or exchange of property which is between members of the same controlled group and to which subsection (a)(1) applies (determined without regard to this paragraph but with regard to paragraph (3))—

(A) subsections (a)(1) and (d) shall not apply to such loss, but

(B) such loss shall be deferred until the property is transferred outside such controlled group and there would be recognition of loss under consolidated return principles or until such other time as may be prescribed in regulations.

(3) Loss deferral rules not to apply in certain cases**(A) Transfer to DISC**

For purposes of applying subsection (a)(1), the term “controlled group” shall not include a DISC.

(B) Certain sales of inventory

Except to the extent provided in regulations prescribed by the Secretary, subsection (a)(1) shall not apply to the sale or exchange of property between members of the same controlled group (or persons described in subsection (b)(10)) if—

(i) such property in the hands of the transferor is property described in section 1221(a)(1),

(ii) such sale or exchange is in the ordinary course of the transferor’s trade or business,

(iii) such property in the hands of the transferee is property described in section 1221(a)(1), and

(iv) the transferee or the transferor is a foreign corporation.

(C) Certain foreign currency losses

To the extent provided in regulations, subsection (a)(1) shall not apply to any loss sus-

tained by a member of a controlled group on the repayment of a loan made to another member of such group if such loan is payable in a foreign currency or is denominated in such a currency and such loss is attributable to a reduction in value of such foreign currency.

(4) Determination of relationship resulting in disallowance of loss, for purposes of other provisions

For purposes of any other section of this title which refers to a relationship which would result in a disallowance of losses under this section, deferral under paragraph (2) shall be treated as disallowance.

(g) Coordination with section 1041

Subsection (a)(1) shall not apply to any transfer described in section 1041(a) (relating to transfers of property between spouses or incident to divorce).

(Aug. 16, 1954, ch. 736, 68A Stat. 78; Pub. L. 95-628, §2(a), Nov. 10, 1978, 92 Stat. 3627; Pub. L. 97-354, §3(h), Oct. 19, 1982, 96 Stat. 1689; Pub. L. 98-369, div. A, title I, §174(a)-(b)(4), title VII, §721(s), July 18, 1984, 98 Stat. 704-707, 970; Pub. L. 99-514, title VIII, §§803(b)(5), 806(c)(2), title XVIII, §§1812(c)(1), (2), (3)(C), (4)(A), 1842(a), Oct. 22, 1986, 100 Stat. 2356, 2364, 2834, 2835, 2852; Pub. L. 100-647, title I, §§1006(e)(9), 1008(e)(6), Nov. 10, 1988, 102 Stat. 3401, 3441; Pub. L. 105-34, title XIII, §1308(a), title XVI, §1604(e)(1), Aug. 5, 1997, 111 Stat. 1041, 1098; Pub. L. 106-170, title V, §532(c)(2)(C), Dec. 17, 1999, 113 Stat. 1930; Pub. L. 108-357, title VIII, §841(b), Oct. 22, 2004, 118 Stat. 1598.)

REFERENCES IN TEXT

Sections 24(b) and 118 of the Internal Revenue Code of 1939, referred to in subsec. (d), were classified to sections 24(b) and 118 of former Title 26, Internal Revenue Code. Sections 24(b) and 118 were repealed by section 7851(a)(1) of this title. For table of comparisons of the 1939 Code to the 1986 Code [formerly I.R.C. 1954], see Table I preceding section 1 of this title. See, also, section 7851(e) of this title for provision that references in the 1986 Code to a provision of the 1939 Code, not then applicable, shall be deemed a reference to the corresponding provision of the 1986 Code, which is then applicable.

AMENDMENTS

2004—Subsec. (a)(3). Pub. L. 108-357 designated existing provisions as subpar. (A), inserted heading, and added subpar. (B).

1999—Subsec. (f)(3)(B)(i), (iii). Pub. L. 106-170 substituted “1221(a)(1)” for “1221(1)”.

1997—Subsec. (b)(13). Pub. L. 105-34, §1308(a), added par. (13).

Subsec. (f)(4). Pub. L. 105-34, §1604(e)(1), added par. (4).

1988—Subsec. (a)(1). Pub. L. 100-647, §1006(e)(9), struck out “(other than a loss in case of a distribution in corporate liquidation)” after “exchange of property” and inserted at end “The preceding sentence shall not apply to any loss of the distributing corporation (or the distributee) in the case of a distribution in complete liquidation.”

Subsec. (a)(2). Pub. L. 100-647, §1008(e)(6), made technical correction to directory language of Pub. L. 99-514, §806(c)(2), see 1986 Amendment note below.

1986—Subsec. (a)(2). Pub. L. 99-514, §806(c)(2), as amended by Pub. L. 100-647, §1008(e)(6), inserted at end “For purposes of this paragraph, in the case of a personal service corporation (within the meaning of sec-

tion 441(i)(2)), such corporation and any employee-owner (within the meaning of section 269A(b)(2), as modified by section 441(i)(2)) shall be treated as persons specified in subsection (b).”

Subsec. (a)(3). Pub. L. 99-514, §1812(c)(1), added par. (3).

Subsec. (b)(12). Pub. L. 99-514, §1812(c)(4)(A), substituted “same persons own” for “same persons owns”.

Subsec. (e)(5)(D). Pub. L. 99-514, §803(b)(5), substituted in cl. (i) “interest in property described in clause (i), (ii), (iii), or (iv) of section 1250(a)(1)(B)” for “interest in low-income housing (as defined in paragraph (5) of section 189(e))” and in cl. (ii) “such property” for “low-income housing (as so defined)”.

Subsec. (e)(6). Pub. L. 99-514, §1812(c)(3)(C), added par. (6).

Subsec. (f)(3)(B). Pub. L. 99-514, §1812(c)(2), inserted “(or persons described in subsection (b)(10))”.

Subsec. (g). Pub. L. 99-514, §1842(a), added subsec. (g).

1984—Subsec. (a). Pub. L. 98-369, §174(a), amended subsec. (a) generally, substituting “In general” for “Deduction disallowed” in heading, “Deduction for losses disallowed” for “Losses” in par. (1) heading, and provisions dealing with matching of deduction and payee income item in the case of expenses and interest for provisions dealing with unpaid expenses and interest in par. (2).

Subsec. (b)(3). Pub. L. 98-369, §174(b)(2)(A), substituted “Two corporations which are members of the same controlled group (as defined in subsection (f))” for “Two corporations more than 50 percent in value of the outstanding stock of each of which is owned, directly or indirectly, by or for the same individual, if either one of such corporations, with respect to the taxable year of the corporation preceding the date of the sale or exchange was, under the law applicable to such taxable year, a personal holding company or a foreign personal holding company”.

Subsec. (b)(10). Pub. L. 98-369, §174(b)(3), substituted “A corporation” for “An S corporation” in introductory provisions and “the corporation” for “the S corporation” in subpar. (A).

Subsec. (b)(12). Pub. L. 98-369, §174(b)(4), substituted “the same persons” for “the same individual”.

Subsec. (e). Pub. L. 98-369, §174(b)(1), added subsec. (e).

Pub. L. 98-369, §174(a)(2), struck out subsec. (e) which provided that for purposes of subsection (a)(2) where the last day of the 2½ month period falls on Saturday, Sunday, or a legal holiday, such last day be treated as falling on the next succeeding day which is not a Saturday, Sunday, or a legal holiday, and the determination of what constitutes a legal holiday be made under section 7503 with respect to the payor’s return of tax under this chapter for the preceding taxable year.

Subsec. (f). Pub. L. 98-369, §174(b)(2)(B), added subsec. (f).

Pub. L. 98-369, §174(b)(1), struck out subsec. (f) which related to special rules for unpaid expenses and interest of S corporations and treatment under such provisions of certain shareholders, etc., as related persons.

Pub. L. 98-369, §721(s), in closing provision of par. (1) substituted “then any deduction allowable under such sections in respect of such amount shall be allowable as of the day as of which such payment is includible in the gross income of the person to whom the payment is made (or, if later, as of the day on which it would be so allowable but for this paragraph)” for “then no deduction shall be allowed in respect of expenses otherwise deductible under section 162 or 212, or of interest otherwise deductible under section 163, before the day as of which the amount thereof is includible in the gross income of the person to whom the payment is made”.

1982—Subsec. (b)(10) to (12). Pub. L. 97-354, §3(h)(1), (3), added pars. (10) to (12).

Subsec. (f). Pub. L. 97-354, §3(h)(2), added subsec. (f). 1978—Subsec. (e). Pub. L. 95-628 added subsec. (e).

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-357 applicable to payments accrued on or after Oct. 22, 2004, see section

841(c) of Pub. L. 108-357, set out as a note under section 163 of this title.

EFFECTIVE DATE OF 1999 AMENDMENT

Amendment by Pub. L. 106-170 applicable to any instrument held, acquired, or entered into, any transaction entered into, and supplies held or acquired on or after Dec. 17, 1999, see section 532(d) of Pub. L. 106-170, set out as a note under section 170 of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Section 1308(c) of Pub. L. 105-34 provided that: “The amendments made by this section [amending this section and section 1239 of this title] shall apply to taxable years beginning after the date of the enactment of this Act [Aug. 5, 1997].”

Section 1604(e)(2) of Pub. L. 105-34 provided that: “The amendment made by paragraph (1) [amending this section] shall take effect as if included in section 174(b) of the Tax Reform Act of 1984 [Pub. L. 98-369].”

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

If any interest costs incurred after Dec. 31, 1986, are attributable to costs incurred before Jan. 1, 1987, the amendment by section 803(b)(5) of Pub. L. 99-514 is applicable to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954 and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of Pub. L. 99-514) or, if applicable, section 266 of such Code, see section 7831(d)(2) of Pub. L. 101-239, set out as an Effective Date note under section 263A of this title.

Amendment by section 803(b)(5) of Pub. L. 99-514 applicable, except as otherwise provided, to costs incurred after Dec. 31, 1986, in taxable years ending after that date, see section 803(d) of Pub. L. 99-514, set out as a note under section 263A of this title.

Amendment by section 806(c)(2) of Pub. L. 99-514 applicable to taxable years beginning after Dec. 31, 1986, with special provisions applicable to taxpayers who are required to change their accounting periods, see section 806(e) of Pub. L. 99-514, set out as a note under section 1378 of this title.

Amendment by sections 1812(c)(1), (2), (3)(C), (4)(A) and 1842(a) of Pub. L. 99-514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98-369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99-514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Section 174(c) of Pub. L. 98-369, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that:

“(1) SUBSECTIONS (a) AND (b)(1).—The amendments made by subsections (a) and (b)(1) [amending this section] shall apply to amounts allowable as deductions under chapter 1 of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] for taxable years beginning after December 31, 1983. For purposes of the preceding sentence, the allowability of a deduction shall be determined without regard to any disallowance or postponement of deductions under section 267 of such Code.

“(2) SUBSECTION (b) (OTHER THAN PARAGRAPH (1)).—“(A) IN GENERAL.—Except as provided in subparagraph (B), the amendments made by subsection (b) (other than paragraph (1) thereof) [amending this section and sections 170, 368, 514, and 1235 of this title] shall apply to transactions after December 31, 1983, in taxable years ending after such date.

“(B) EXCEPTION FOR TRANSFERS TO FOREIGN CORPORATIONS ON OR BEFORE MARCH 1, 1984.—The amendments made by subsection (b)(2) [amending this section] shall not apply to property transferred to a foreign corporation on or before March 1, 1984.

“(3) EXCEPTION FOR EXISTING INDEBTEDNESS, ETC.—

“(A) IN GENERAL.—The amendments made by this section [amending this section and sections 170, 368, 514, and 1235 of this title] shall not apply to any amount paid or incurred—

“(i) on indebtedness incurred on or before September 29, 1983, or

“(ii) pursuant to a contract which was binding on September 29, 1983, and at all times thereafter before the amount is paid or incurred.

“(B) TREATMENT OF RENEGOTIATIONS, EXTENSIONS, ETC.—If any indebtedness (or contract described in subparagraph (A)) is renegotiated, extended, renewed, or revised after September 29, 1983, subparagraph (A) shall not apply to any amount paid or incurred on such indebtedness (or pursuant to such contract) after the date of such renegotiation, extension, renewal, or revision.”

Amendment by section 721(s) of Pub. L. 98-369 effective as if included in the Subchapter S Revision Act of 1982, Pub. L. 97-354, see section 721(y)(1) of Pub. L. 98-369, set out as a note under section 1361 of this title.

EFFECTIVE DATE OF 1982 AMENDMENT

Amendment by Pub. L. 97-354 applicable to taxable years beginning after Dec. 31, 1982, see section 6(a) of Pub. L. 97-354, set out as an Effective Date note under section 1361 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Section 2(b) of Pub. L. 95-628 provided that: “The amendment made by subsection (a) [amending this section] shall apply with respect to payments made after the date of the enactment of this Act [Nov. 10, 1978].”

CONSTRUCTION OF SECTION 806 OF PUB. L. 99-514

Nothing in section 806 of Pub. L. 99-514 [amending this section] or in any legislative history relating thereto to be construed as requiring the Secretary of the Treasury or his delegate to permit an automatic change of a taxable year, see section 1008(e)(9) of Pub. L. 100-647, set out as a note under section 1378 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101-1147 and 1171-1177] or title XVIII [§§ 1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

EXCEPTION FOR CERTAIN INDEBTEDNESS

Section 1812(c)(5) of Pub. L. 99-514 provided that: “Clause (i) of section 174(c)(3)(A) of the Tax Reform Act of 1984 [section 174(c)(3)(A)(i) of Pub. L. 98-369, set out as a note above] shall be applied by substituting ‘December 31, 1983’ for ‘September 29, 1983’ in the case of indebtedness which matures on January 1, 1999, the payments on which from January 1989 through November 1993 equal U/L plus \$77,600, the payments on which from December 1993 to maturity equal U/L plus \$50,100, and which accrued interest at 13.75 percent through December 31, 1989.”

§ 268. Sale of land with unharvested crop

Where an unharvested crop sold by the taxpayer is considered under the provisions of section 1231 as “property used in the trade or business”, in computing taxable income no deduc-

tion (whether or not for the taxable year of the sale and whether for expenses, depreciation, or otherwise) attributable to the production of such crop shall be allowed.

(Aug. 16, 1954, ch. 736, 68A Stat. 80.)

§ 269. Acquisitions made to evade or avoid income tax

(a) In general

If—

(1) any person or persons acquire, or acquired on or after October 8, 1940, directly or indirectly, control of a corporation, or

(2) any corporation acquires, or acquired on or after October 8, 1940, directly or indirectly, property of another corporation, not controlled, directly or indirectly, immediately before such acquisition, by such acquiring corporation or its stockholders, the basis of which property, in the hands of the acquiring corporation, is determined by reference to the basis in the hands of the transferor corporation,

and the principal purpose for which such acquisition was made is evasion or avoidance of Federal income tax by securing the benefit of a deduction, credit, or other allowance which such person or corporation would not otherwise enjoy, then the Secretary may disallow such deduction, credit, or other allowance. For purposes of paragraphs (1) and (2), control means the ownership of stock possessing at least 50 percent of the total combined voting power of all classes of stock entitled to vote or at least 50 percent of the total value of shares of all classes of stock of the corporation.

(b) Certain liquidations after qualified stock purchases

(1) In general

If—

(A) there is a qualified stock purchase by a corporation of another corporation,

(B) an election is not made under section 338 with respect to such purchase,

(C) the acquired corporation is liquidated pursuant to a plan of liquidation adopted not more than 2 years after the acquisition date, and

(D) the principal purpose for such liquidation is the evasion or avoidance of Federal income tax by securing the benefit of a deduction, credit, or other allowance which the acquiring corporation would not otherwise enjoy,

then the Secretary may disallow such deduction, credit, or other allowance.

(2) Meaning of terms

For purposes of paragraph (1), the terms “qualified stock purchase” and “acquisition date” have the same respective meanings as when used in section 338.

(c) Power of Secretary to allow deduction, etc., in part

In any case to which subsection (a) or (b) applies the Secretary is authorized—

(1) to allow as a deduction, credit, or allowance any part of any amount disallowed by

such subsection, if he determines that such allowance will not result in the evasion or avoidance of Federal income tax for which the acquisition was made; or

(2) to distribute, apportion, or allocate gross income, and distribute, apportion, or allocate the deductions, credits, or allowances the benefit of which was sought to be secured, between or among the corporations, or properties, or parts thereof, involved, and to allow such deductions, credits, or allowances so distributed, apportioned, or allocated, but to give effect to such allowance only to such extent as he determines will not result in the evasion or avoidance of Federal income tax for which the acquisition was made; or

(3) to exercise his powers in part under paragraph (1) and in part under paragraph (2).

(Aug. 16, 1954, ch. 736, 68A Stat. 80; Pub. L. 88-272, title II, §235(c)(2), Feb. 26, 1964, 78 Stat. 126; Pub. L. 94-455, title XIX, §§1901(a)(38), 1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1771, 1834; Pub. L. 98-369, div. A, title VII, §712(k)(8)(A), (B), July 18, 1984, 98 Stat. 952.)

AMENDMENTS

1984—Subsecs. (b), (c). Pub. L. 98-369 added subsec. (b), redesignated former subsec. (b) as (c) and inserted reference to subsec. (b).

1976—Subsecs. (a), (b). Pub. L. 94-455, §1906(b)(13)(A), struck out “or his delegate” after “Secretary” whenever appearing.

Subsec. (c). Pub. L. 94-455, §1901(a)(38), struck out subsec. (c) relating to presumptions in the case of disproportionate purchase price.

1964—Subsec. (a). Pub. L. 88-272 substituted “the Secretary or his delegate may disallow such deduction, credit, or other allowance” for “such deduction, credit or other allowance shall not be allowed”.

EFFECTIVE DATE OF 1984 AMENDMENT

Section 712(k)(8)(C) of Pub. L. 98-369 provided that: “The amendments made by this paragraph [amending this section] shall apply to liquidations after October 20, 1983, in taxable years ending after such date.”

EFFECTIVE DATE OF 1964 AMENDMENT

Amendment by Pub. L. 88-272 applicable to taxable years ending after Dec. 31, 1963, see section 235(d) of Pub. L. 88-272, set out as a note under section 1551 of this title.

§ 269A. Personal service corporations formed or availed of to avoid or evade income tax

(a) General rule

If—

(1) substantially all of the services of a personal service corporation are performed for (or on behalf of) 1 other corporation, partnership, or other entity, and

(2) the principal purpose for forming, or availing of, such personal service corporation is the avoidance or evasion of Federal income tax by reducing the income of, or securing the benefit of any expense, deduction, credit, exclusion, or other allowance for, any employee-owner which would not otherwise be available,

then the Secretary may allocate all income, deductions, credits, exclusions, and other allowances between such personal service corporation and its employee-owners, if such allocation is necessary to prevent avoidance or evasion of

Federal income tax or clearly to reflect the income of the personal service corporation or any of its employee-owners.

(b) Definitions

For purposes of this section—

(1) Personal service corporation

The term “personal service corporation” means a corporation the principal activity of which is the performance of personal services and such services are substantially performed by employee-owners.

(2) Employee-owner

The term “employee-owner” means any employee who owns, on any day during the taxable year, more than 10 percent of the outstanding stock of the personal service corporation. For purposes of the preceding sentence, section 318 shall apply, except that “5 percent” shall be substituted for “50 percent” in section 318(a)(2)(C).

(3) Related persons

All related persons (within the meaning of section 144(a)(3)) shall be treated as 1 entity.

(Added Pub. L. 97-248, title II, §250(a), Sept. 3, 1982, 96 Stat. 528; amended Pub. L. 99-514, title XIII, §1301(j)(4), Oct. 22, 1986, 100 Stat. 2657.)

AMENDMENTS

1986—Subsec. (b)(3). Pub. L. 99-514 substituted “section 144(a)(3)” for “section 103(b)(6)(C)”.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99-514 applicable to bonds issued after Aug. 15, 1986, except as otherwise provided, see sections 1311 to 1318 of Pub. L. 99-514, set out as an Effective Date; Transitional Rules note under section 141 of this title.

EFFECTIVE DATE

Section 250(c) of Pub. L. 97-248 provided that: “The amendments made by this section [enacting this section] shall apply to taxable years beginning after December 31, 1982.”

§ 269B. Stapled entities

(a) General rule

Except as otherwise provided by regulations, for purposes of this title—

(1) if a domestic corporation and a foreign corporation are stapled entities, the foreign corporation shall be treated as a domestic corporation.

(2) in applying section 1563, stock in a second corporation which constitutes a stapled interest with respect to stock of a first corporation shall be treated as owned by such first corporation, and

(3) in applying subchapter M for purposes of determining whether any stapled entity is a regulated investment company or a real estate investment trust, all entities which are stapled entities with respect to each other shall be treated as 1 entity.

(b) Secretary to prescribe regulations

The Secretary shall prescribe such regulations as may be necessary to prevent avoidance or evasion of Federal income tax through the use of stapled entities. Such regulations may in-

clude (but shall not be limited to) regulations providing the extent to which 1 of such entities shall be treated as owning the other entity (to the extent of the stapled interest) and regulations providing that any tax imposed on the foreign corporation referred to in subsection (a)(1) may, if not paid by such corporation, be collected from the domestic corporation referred to in such subsection or the shareholders of such foreign corporation.

(c) Definitions

For purposes of this section—

(1) Entity

The term “entity” means any corporation, partnership, trust, association, estate, or other form of carrying on a business or activity.

(2) Stapled entities

The term “stapled entities” means any group of 2 or more entities if more than 50 percent in value of the beneficial ownership in each of such entities consists of stapled interests.

(3) Stapled interests

Two or more interests are stapled interests if, by reason of form of ownership, restrictions on transfer, or other terms or conditions, in connection with the transfer of 1 of such interests the other such interests are also transferred or required to be transferred.

(d) Special rule for treaties

Nothing in section 894 or 7852(d) or in any other provision of law shall be construed as permitting an exemption, by reason of any treaty obligation of the United States heretofore or hereafter entered into, from the provisions of this section.

(e) Subsection (a)(1) not to apply in certain cases

(1) In general

Subsection (a)(1) shall not apply if it is established to the satisfaction of the Secretary that the domestic corporation and the foreign corporation referred to in such subsection are foreign owned.

(2) Foreign owned

For purposes of paragraph (1), a corporation is foreign owned if less than 50 percent of—

(A) the total combined voting power of all classes of stock of such corporation entitled to vote, and

(B) the total value of the stock of the corporation,

is held directly (or indirectly through applying paragraphs (2) and (3) of section 958(a) and paragraph (4) of section 318(a)) by United States persons (as defined in section 7701(a)(30)).

(Added Pub. L. 98-369, div. A, title I, §136(a), July 18, 1984, 98 Stat. 669; amended Pub. L. 99-514, title XVIII, §1810(j), Oct. 22, 1986, 100 Stat. 2829.)

AMENDMENTS

1986—Subsec. (b). Pub. L. 99-514, §1810(j)(1), inserted “and regulations providing that any tax imposed on the

foreign corporation referred to in subsection (a)(1) may, if not paid by such corporation, be collected from the domestic corporation referred to in such subsection or the shareholders of such foreign corporation”.

Subsec. (e). Pub. L. 99-514, §1810(j)(2), added subsec. (e).

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99-514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98-369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99-514, set out as a note under section 48 of this title.

EFFECTIVE DATE

Section 136(c) of Pub. L. 98-369, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that:

“(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [enacting this section] shall take effect on the date of the enactment of this Act [July 18, 1984].

“(2) INTERESTS STAPLED AS OF JUNE 30, 1983.—Except as otherwise provided in this subsection, in the case of any interests which on June 30, 1983, were stapled interests (as defined in section 269B(c)(3) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (as added by this section)), the amendments made by this section shall take effect on January 1, 1985 (January 1, 1987, in the case of stapled interests in a foreign corporation).

“(3) CERTAIN STAPLED ENTITIES WHICH INCLUDE REAL ESTATE INVESTMENT TRUST.—Paragraph (3) of section 269B(a) of such Code shall not apply in determining the application of the provisions of part II of subchapter M of chapter 1 of such Code to any real estate investment trust which is part of a group of stapled entities if—

“(A) all members of such group were stapled entities as of June 30, 1983, and

“(B) as of June 30, 1983, such group included one or more real estate investment trusts.

“(4) CERTAIN STAPLED ENTITIES WHICH INCLUDE PUERTO RICAN CORPORATIONS.—

“(A) Paragraph (1) of section 269B(a) of such Code shall not apply to a domestic corporation and a qualified Puerto Rican corporation which, on June 30, 1983, were stapled entities.

“(B) For purposes of subparagraph (A), the term ‘qualified Puerto Rican corporation’ means any corporation organized in Puerto Rico—

“(i) which is described in section 957(c) of such Code or would be so described if any dividends it received from any other corporation described in such section 957(c) were treated as gross income of the type described in such section 957(c), and

“(ii) does not, at any time during the taxable year, own (within the meaning of section 958 of such Code but before applying paragraph (2) of section 269B(a) of such Code) any stock of any corporation which is not described in such section 957(c).

“(5) TREATY RULE NOT TO APPLY TO STAPLED ENTITIES ENTITLED TO TREATY BENEFITS AS OF JUNE 30, 1983.—In the case of any entity which was a stapled entity as of June 30, 1983, subsection (d) of section 269B of such Code shall not apply to any treaty benefit to which such entity was entitled as of June 30, 1983.

“(6) ELECTIONS TO TREAT STAPLED FOREIGN ENTITIES AS SUBSIDIARIES.—

“(A) IN GENERAL.—In the case of any foreign corporation and domestic corporation which as of June 30, 1983, were stapled entities, such domestic corporation may elect (in lieu of applying paragraph (1) of section 269B(a) of such Code) to be treated as owning all interests in the foreign corporation which constitute stapled interests with respect to stock of the domestic corporation.

“(B) ELECTION.—Any election under subparagraph (A) shall be made not later than 180 days after the date of the enactment of this Act and shall be made in such manner as the Secretary of the Treasury or his delegate shall prescribe.

“(C) ELECTION IRREVOCABLE.—Any election under subparagraph (A), once made, may be revoked only with the consent of the Secretary of the Treasury or his delegate.

“(7) OTHER STAPLED ENTITIES WHICH INCLUDE REAL ESTATE INVESTMENT TRUST.—

“(A) IN GENERAL.—Paragraph (3) of section 269B(a) of such Code shall not apply in determining the application of the provisions of part II of subchapter M of chapter 1 of such Code to any qualified real estate investment trust which is a part of a group of stapled entities—

“(i) which was created pursuant to a written board of directors resolution adopted on April 5, 1984, and

“(ii) all members of such group were stapled entities as of June 16, 1985.

“(B) QUALIFIED REAL ESTATE INVESTMENT TRUST.—The term ‘qualified real estate investment trust’ means any real estate trust—

“(i) at least 75 percent of the gross income of which is derived from interest on obligations secured by mortgages on real property (as defined in section 856 of such Code),

“(ii) with respect to which the interest on the obligations described in clause (i) made or acquired by such trust (other than to persons who are independent contractors, as defined in section 856(d)(3) of such Code) is at an arm’s length rate or a rate not more than 1 percentage point greater than the associated borrowing cost of the trust, and

“(iii) with respect to which any real property held by the trust is not used in the trade or business of any other member of the group of stapled entities.”

TERMINATION OF EXCEPTION FOR CERTAIN REAL ESTATE INVESTMENT TRUSTS FROM THE TREATMENT OF STAPLED ENTITIES

Pub. L. 105-206, title VII, §7002, July 22, 1998, 112 Stat. 827, provided that:

“(a) IN GENERAL.—Notwithstanding paragraph (3) of section 136(c) of the Tax Reform Act of 1984 [Pub. L. 98-369, set out above] (relating to stapled stock; stapled entities), the REIT gross income provisions shall be applied by treating the activities and gross income of members of the stapled REIT group properly allocable to any nonqualified real property interest held by the exempt REIT or any stapled entity which is a member of such group (or treated under subsection (c) as held by such REIT or stapled entity) as the activities and gross income of the exempt REIT in the same manner as if the exempt REIT and such group were one entity.

“(b) NONQUALIFIED REAL PROPERTY INTEREST.—For purposes of this section—

“(1) IN GENERAL.—The term ‘nonqualified real property interest’ means, with respect to any exempt REIT, any interest in real property acquired after March 26, 1998, by the exempt REIT or any stapled entity.

“(2) EXCEPTION FOR BINDING CONTRACTS, ETC.—Such term shall not include any interest in real property acquired after March 26, 1998, by the exempt REIT or any stapled entity if—

“(A) the acquisition is pursuant to a written agreement (including a put option, buy-sell agreement, and an agreement relating to a third party default) which was binding on such date and at all times thereafter on such REIT or stapled entity; or

“(B) the acquisition is described on or before such date in a public announcement or in a filing with the Securities and Exchange Commission.

“(3) IMPROVEMENTS AND LEASES.—

“(A) IN GENERAL.—Except as otherwise provided in this paragraph, the term ‘nonqualified real property interest’ shall not include—

“(i) any improvement to land owned or leased by the exempt REIT or any member of the stapled REIT group; and

“(ii) any repair to, or improvement of, any improvement owned or leased by the exempt REIT or any member of the stapled REIT group,

if such ownership or leasehold interest is a qualified real property interest.

“(B) LEASES.—The term ‘nonqualified real property interest’ shall not include—

“(i) any lease of a qualified real property interest if such lease is not otherwise such an interest; or

“(ii) any renewal of a lease which is a qualified real property interest,

but only if the rent on any lease referred to in clause (i) or any renewal referred to in clause (ii) does not exceed an arm’s length rate.

“(C) TERMINATION WHERE CHANGE IN USE.—

“(i) IN GENERAL.—Subparagraph (A) shall not apply to any improvement placed in service after December 31, 1999, which is part of a change in the use of the property to which such improvement relates unless the cost of such improvement does not exceed 200 percent of—

“(I) the cost of such property; or

“(II) if such property is substituted basis property (as defined in section 7701(a)(42) of the Internal Revenue Code of 1986), the fair market value of the property at the time of acquisition.

“(ii) BINDING CONTRACTS.—For purposes of clause (i), an improvement shall be treated as placed in service before January 1, 2000, if such improvement is placed in service before January 1, 2004, pursuant to a binding contract in effect on December 31, 1999, and at all times thereafter.

“(4) EXCEPTION FOR PERMITTED TRANSFERS, ETC.—The term ‘nonqualified real property interest’ shall not include any interest in real property acquired solely as a result of a direct or indirect contribution, distribution, or other transfer of such interest from the exempt REIT or any member of the stapled REIT group to such REIT or any such member, but only to the extent the aggregate of the interests of the exempt REIT and all stapled entities in such interest in real property (determined in accordance with subsection (c)(1)) is not increased by reason of the transfer.

“(5) TREATMENT OF ENTITIES WHICH ARE NOT STAPLED, ETC. ON MARCH 26, 1998.—Notwithstanding any other provision of this section, all interests in real property held by an exempt REIT or any stapled entity with respect to such REIT (or treated under subsection (c) as held by such REIT or stapled entity) shall be treated as nonqualified real property interests unless—

“(A) such stapled entity was a stapled entity with respect to such REIT as of March 26, 1998, and at all times thereafter; and

“(B) as of March 26, 1998, and at all times thereafter, such REIT was a real estate investment trust.

“(6) QUALIFIED REAL PROPERTY INTEREST.—The term ‘qualified real property interest’ means any interest in real property other than a nonqualified real property interest.

“(c) TREATMENT OF PROPERTY HELD BY 10-PERCENT SUBSIDIARIES.—For purposes of this section—

“(1) IN GENERAL.—Any exempt REIT and any stapled entity shall be treated as holding their proportionate shares of each interest in real property held by any 10-percent subsidiary entity of the exempt REIT or stapled entity, as the case may be.

“(2) PROPERTY HELD BY 10-PERCENT SUBSIDIARIES TREATED AS NONQUALIFIED.—

“(A) IN GENERAL.—Except as provided in subparagraph (B), any interest in real property held by a 10-percent subsidiary entity of an exempt REIT or stapled entity shall be treated as a nonqualified real property interest.

“(B) EXCEPTION FOR INTERESTS IN REAL PROPERTY HELD ON MARCH 26, 1998, ETC.—In the case of an entity which was a 10-percent subsidiary entity of an exempt REIT or stapled entity on March 26, 1998, and at all times thereafter, an interest in real property held by such subsidiary entity shall be treated as a

qualified real property interest if such interest would be so treated if held or acquired directly by the exempt REIT or the stapled entity.

“(3) REDUCTION IN QUALIFIED REAL PROPERTY INTERESTS IF INCREASE IN OWNERSHIP OF SUBSIDIARY.—If, after March 26, 1998, an exempt REIT or stapled entity increases its ownership interest in a subsidiary entity to which paragraph (2)(B) applies above its ownership interest in such subsidiary entity as of such date, the additional portion of each interest in real property which is treated as held by the exempt REIT or stapled entity by reason of such increased ownership shall be treated as a nonqualified real property interest.

“(4) SPECIAL RULES FOR DETERMINING OWNERSHIP.—For purposes of this subsection—

“(A) percentage ownership of an entity shall be determined in accordance with subsection (e)(4);

“(B) interests in the entity which are acquired by an exempt REIT or a member of the stapled REIT group in any acquisition described in an agreement, announcement, or filing described in subsection (b)(2) shall be treated as acquired on March 26, 1998; and

“(C) except as provided in guidance prescribed by the Secretary, any change in proportionate ownership which is attributable solely to fluctuations in the relative fair market values of different classes of stock shall not be taken into account.

“(5) TREATMENT OF 60-PERCENT PARTNERSHIPS.—

“(A) IN GENERAL.—If, as of March 26, 1998—

“(i) an exempt REIT or stapled entity held directly or indirectly at least 60 percent of the capital or profits interest in a partnership; and

“(ii) 90 percent or more of the capital interests and 90 percent or more of the profits interests in such partnership (other than interests held directly or indirectly by the exempt REIT or stapled entity) are, or will be, redeemable or exchangeable for consideration the amount of which is determined by reference to the value of shares of stock in the exempt REIT or stapled entity (or both),

paragraph (3) shall not apply to such partnership, and such REIT or entity shall be treated for all purposes of this section as holding all of the capital and profits interests in such partnership.

“(B) LIMITATION TO ONE PARTNERSHIP.—If, as of January 1, 1999, more than one partnership owned by any exempt REIT or stapled entity meets the requirements of subparagraph (A), only the largest such partnership on such date (determined by aggregate asset bases) shall be treated as meeting such requirements.

“(C) MIRROR ENTITY.—For purposes of subparagraph (A), an interest in a partnership formed after March 26, 1998, shall be treated as held by an exempt REIT or stapled entity on March 26, 1998, if such partnership is formed to mirror the stapling of an exempt REIT and a stapled entity in connection with an acquisition agreed to or announced on or before March 26, 1998.

“(d) TREATMENT OF PROPERTY SECURED BY MORTGAGE HELD BY EXEMPT REIT OR MEMBER OF STAPLED REIT GROUP.—

“(1) IN GENERAL.—In the case of any nonqualified obligation held by an exempt REIT or any member of the stapled REIT group, the REIT gross income provisions shall be applied by treating the exempt REIT as having impermissible tenant service income equal to—

“(A) the interest income from such obligation which is properly allocable to the property described in paragraph (2); and

“(B) the income of any member of the stapled REIT group from services described in paragraph (2) with respect to such property.

If the income referred to in subparagraph (A) or (B) is of a 10-percent subsidiary entity, only the portion of such income which is properly allocable to the ex-

empt REIT's or the stapled entity's interest in the subsidiary entity shall be taken into account.

“(2) NONQUALIFIED OBLIGATION.—Except as otherwise provided in this subsection, the term ‘nonqualified obligation’ means any obligation secured by a mortgage on an interest in real property if the income of any member of the stapled REIT group for services furnished with respect to such property would be impermissible tenant service income were such property held by the exempt REIT and such services furnished by the exempt REIT.

“(3) EXCEPTION FOR CERTAIN MARKET RATE OBLIGATIONS.—Such term shall not include any obligation—

“(A) payments under which would be treated as interest if received by a REIT; and

“(B) the rate of interest on which does not exceed an arm's length rate.

“(4) EXCEPTION FOR EXISTING OBLIGATIONS.—Such term shall not include any obligation—

“(A) which is secured on March 26, 1998, by an interest in real property; and

“(B) which is held on such date by the exempt REIT or any entity which is a member of the stapled REIT group on such date and at all times thereafter,

but only so long as such obligation is secured by such interest, and the interest payable on such obligation is not changed to a rate which exceeds an arm's length rate unless such change is pursuant to the terms of the obligation in effect on March 26, 1998. The preceding sentence shall not cease to apply by reason of the refinancing of the obligation if (immediately after the refinancing) the principal amount of the obligation resulting from the refinancing does not exceed the principal amount of the refinanced obligation (immediately before the refinancing) and the interest payable on such refinanced obligation does not exceed an arm's length rate.

“(5) TREATMENT OF ENTITIES WHICH ARE NOT STAPLED, ETC. ON MARCH 26, 1998.—A rule similar to the rule of subsection (b)(5) shall apply for purposes of this subsection.

“(6) INCREASE IN AMOUNT OF NONQUALIFIED OBLIGATIONS IF INCREASE IN OWNERSHIP OF SUBSIDIARY.—A rule similar to the rule of subsection (c)(3) shall apply for purposes of this subsection.

“(7) COORDINATION WITH SUBSECTION (a).—This subsection shall not apply to the portion of any interest in real property that the exempt REIT or stapled entity holds or is treated as holding under this section without regard to this subsection.

“(e) DEFINITIONS.—For purposes of this section—

“(1) REIT GROSS INCOME PROVISIONS.—The term ‘REIT gross income provisions’ means—

“(A) paragraphs (2), (3), and (6) of section 856(c) of the Internal Revenue Code of 1986; and

“(B) section 857(b)(5) of such Code.

“(2) EXEMPT REIT.—The term ‘exempt REIT’ means a real estate investment trust to which section 269B of the Internal Revenue Code of 1986 does not apply by reason of paragraph (3) of section 136(c) of the Tax Reform Act of 1984.

“(3) STAPLED REIT GROUP.—The term ‘stapled REIT group’ means, with respect to an exempt REIT, the group consisting of—

“(A) all entities which are stapled entities with respect to the exempt REIT; and

“(B) all entities which are 10-percent subsidiary entities of the exempt REIT or any such stapled entity.

“(4) 10-PERCENT SUBSIDIARY ENTITY.—

“(A) IN GENERAL.—The term ‘10-percent subsidiary entity’ means, with respect to any exempt REIT or stapled entity, any entity in which the exempt REIT or stapled entity (as the case may be) directly or indirectly holds at least a 10-percent interest.

“(B) EXCEPTION FOR CERTAIN C CORPORATION SUBSIDIARIES OF REITS.—A corporation which would, but for this subparagraph, be treated as a 10-per-

cent subsidiary of an exempt REIT shall not be so treated if such corporation is taxable under section 11 of the Internal Revenue Code of 1986.

“(C) 10-PERCENT INTEREST.—The term ‘10-percent interest’ means—

“(i) in the case of an interest in a corporation, ownership of 10 percent (by vote or value) of the stock in such corporation;

“(ii) in the case of an interest in a partnership, ownership of 10 percent of the capital or profits interest in the partnership; and

“(iii) in any other case, ownership of 10 percent of the beneficial interests in the entity.

“(5) OTHER DEFINITIONS.—Terms used in this section which are used in section 269B or section 856 of such Code shall have the respective meanings given such terms by such section.

“(f) GUIDANCE.—The Secretary may prescribe such guidance as may be necessary or appropriate to carry out the purposes of this section, including guidance to prevent the avoidance of such purposes and to prevent the double counting of income.

“(g) EFFECTIVE DATE.—This section shall apply to taxable years ending after March 26, 1998.”

PLAN AMENDMENTS NOT REQUIRED UNTIL
JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

[§ 270. Repealed. Pub. L. 91-172, title II, § 213(b), Dec. 30, 1969, 83 Stat. 572]

Section, act Aug. 16, 1954, ch. 736, 68A Stat. 81, related to the limitation on deductions allowable to certain individuals. See section 183 of this title.

EFFECTIVE DATE OF REPEAL

Repeal applicable to taxable years beginning after Dec. 31, 1969, see section 213(d) of Pub. L. 91-172, set out as an Effective Date note under section 183 of this title.

§ 271. Debts owed by political parties, etc.

(a) General rule

In the case of a taxpayer (other than a bank as defined in section 581) no deduction shall be allowed under section 166 (relating to bad debts) or under section 165(g) (relating to worthlessness of securities) by reason of the worthlessness of any debt owed by a political party.

(b) Definitions

(1) Political party

For purposes of subsection (a), the term “political party” means—

(A) a political party;

(B) a national, State, or local committee of a political party; or

(C) a committee, association, or organization which accepts contributions or makes expenditures for the purpose of influencing or attempting to influence the election of presidential or vice-presidential electors or of any individual whose name is presented for election to any Federal, State, or local elective public office, whether or not such individual is elected.

(2) Contributions

For purposes of paragraph (1)(C), the term “contributions” includes a gift, subscription,

loan, advance, or deposit, of money, or anything of value, and includes a contract, promise, or agreement to make a contribution, whether or not legally enforceable.

(3) Expenditures

For purposes of paragraph (1)(C), the term “expenditures” includes a payment, distribution, loan, advance, deposit, or gift, of money, or anything of value, and includes a contract, promise, or agreement to make an expenditure, whether or not legally enforceable.

(c) Exception

In the case of a taxpayer who uses an accrual method of accounting, subsection (a) shall not apply to a debt which accrued as a receivable on a bona fide sale of goods or services in the ordinary course of the taxpayer’s trade or business if—

(1) for the taxable year in which such receivable accrued, more than 30 percent of all receivables which accrued in the ordinary course of the trades and businesses of the taxpayer were due from political parties, and

(2) the taxpayer made substantial continuing efforts to collect on the debt.

(Aug. 16, 1954, ch. 736, 68A Stat. 82; Pub. L. 94-455, title XXI, § 2104(a), Oct. 4, 1976, 90 Stat. 1901.)

AMENDMENTS

1976—Subsec. (c). Pub. L. 94-455 added subsec. (c).

EFFECTIVE DATE OF 1976 AMENDMENT

Section 2104(b) of Pub. L. 94-455 provided that: “The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1975.”

§ 272. Disposal of coal or domestic iron ore

Where the disposal of coal or iron ore is covered by section 631, no deduction shall be allowed for expenditures attributable to the making and administering of the contract under which such disposition occurs and to the preservation of the economic interest retained under such contract, except that if in any taxable year such expenditures plus the adjusted depletion basis of the coal or iron ore disposed of in such taxable year exceed the amount realized under such contract, such excess, to the extent not availed of as a reduction of gain under section 1231, shall be a loss deductible under section 165(a). This section shall not apply to any taxable year during which there is no income under the contract.

(Aug. 16, 1954, ch. 736, 68A Stat. 82; Pub. L. 88-272, title II, § 227(a)(3), (b)(3), Feb. 26, 1964, 78 Stat. 98.)

AMENDMENTS

1964—Pub. L. 88-272 inserted “or domestic iron ore” in section catchline, and “or iron ore” wherever appearing in text.

EFFECTIVE DATE OF 1964 AMENDMENT

Section 227(c) of Pub. L. 88-272 provided that: “The amendments made by this section [amending this section and sections 631, 1016, 1231, and 1402 and section 411 of Title 42, The Public Health and Welfare] shall apply with respect to amounts received or accrued in taxable years beginning after December 31, 1963, attributable to iron ore mined in such taxable years.”

§ 273. Holders of life or terminable interest

Amounts paid under the laws of a State, the District of Columbia, a possession of the United States, or a foreign country as income to the holder of a life or terminable interest acquired by gift, bequest, or inheritance shall not be reduced or diminished by any deduction for shrinkage (by whatever name called) in the value of such interest due to the lapse of time. (Aug. 16, 1954, ch. 736, 68A Stat. 83; Pub. L. 94-455, title XIX, §1901(c)(2), Oct. 4, 1976, 90 Stat. 1803.)

AMENDMENTS

1976—Pub. L. 94-455 struck out reference to amounts paid under laws of a Territory.

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by Pub. L. 94-455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94-455, set out as a note under section 2 of this title.

§ 274. Disallowance of certain entertainment, etc., expenses**(a) Entertainment, amusement, or recreation****(1) In general**

No deduction otherwise allowable under this chapter shall be allowed for any item—

(A) Activity

With respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, unless the taxpayer establishes that the item was directly related to, or, in the case of an item directly preceding or following a substantial and bona fide business discussion (including business meetings at a convention or otherwise), that such item was associated with, the active conduct of the taxpayer's trade or business, or

(B) Facility

With respect to a facility used in connection with an activity referred to in subparagraph (A).

In the case of an item described in subparagraph (A), the deduction shall in no event exceed the portion of such item which meets the requirements of subparagraph (A).

(2) Special rules

For purposes of applying paragraph (1)—

(A) Dues or fees to any social, athletic, or sporting club or organization shall be treated as items with respect to facilities.

(B) An activity described in section 212 shall be treated as a trade or business.

(C) In the case of a club, paragraph (1)(B) shall apply unless the taxpayer establishes that the facility was used primarily for the furtherance of the taxpayer's trade or business and that the item was directly related to the active conduct of such trade or business.

(3) Denial of deduction for club dues

Notwithstanding the preceding provisions of this subsection, no deduction shall be allowed under this chapter for amounts paid or incurred for membership in any club organized

for business, pleasure, recreation, or other social purpose.

(b) Gifts**(1) Limitation**

No deduction shall be allowed under section 162 or section 212 for any expense for gifts made directly or indirectly to any individual to the extent that such expense, when added to prior expenses of the taxpayer for gifts made to such individual during the same taxable year, exceeds \$25. For purposes of this section, the term "gift" means any item excludable from gross income of the recipient under section 102 which is not excludable from his gross income under any other provision of this chapter, but such term does not include—

(A) an item having a cost to the taxpayer not in excess of \$4.00 on which the name of the taxpayer is clearly and permanently imprinted and which is one of a number of identical items distributed generally by the taxpayer, or

(B) a sign, display rack, or other promotional material to be used on the business premises of the recipient.

(2) Special rules

(A) In the case of a gift by a partnership, the limitation contained in paragraph (1) shall apply to the partnership as well as to each member thereof.

(B) For purposes of paragraph (1), a husband and wife shall be treated as one taxpayer.

(c) Certain foreign travel**(1) In general**

In the case of any individual who travels outside the United States away from home in pursuit of a trade or business or in pursuit of an activity described in section 212, no deduction shall be allowed under section 162, or section 212 for that portion of the expenses of such travel otherwise allowable under such section which, under regulations prescribed by the Secretary, is not allocable to such trade or business or to such activity.

(2) Exception

Paragraph (1) shall not apply to the expenses of any travel outside the United States away from home if—

(A) such travel does not exceed one week, or

(B) the portion of the time of travel outside the United States away from home which is not attributable to the pursuit of the taxpayer's trade or business or an activity described in section 212 is less than 25 percent of the total time on such travel.

(3) Domestic travel excluded

For purposes of this subsection, travel outside the United States does not include any travel from one point in the United States to another point in the United States.

(d) Substantiation required

No deduction or credit shall be allowed—

(1) under section 162 or 212 for any traveling expense (including meals and lodging while away from home),

(2) for any item with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, or with respect to a facility used in connection with such an activity,

(3) for any expense for gifts, or

(4) with respect to any listed property (as defined in section 280F(d)(4)),

unless the taxpayer substantiates by adequate records or by sufficient evidence corroborating the taxpayer's own statement (A) the amount of such expense or other item, (B) the time and place of the travel, entertainment, amusement, recreation, or use of the facility or property, or the date and description of the gift, (C) the business purpose of the expense or other item, and (D) the business relationship to the taxpayer of persons entertained, using the facility or property, or receiving the gift. The Secretary may by regulations provide that some or all of the requirements of the preceding sentence shall not apply in the case of an expense which does not exceed an amount prescribed pursuant to such regulations. This subsection shall not apply to any qualified nonpersonal use vehicle (as defined in subsection (i)).

(e) Specific exceptions to application of subsection (a)

Subsection (a) shall not apply to—

(1) Food and beverages for employees

Expenses for food and beverages (and facilities used in connection therewith) furnished on the business premises of the taxpayer primarily for his employees.

(2) Expenses treated as compensation

(A) In general

Except as provided in subparagraph (B), expenses for goods, services, and facilities, to the extent that the expenses are treated by the taxpayer, with respect to the recipient of the entertainment, amusement, or recreation, as compensation to an employee on the taxpayer's return of tax under this chapter and as wages to such employee for purposes of chapter 24 (relating to withholding of income tax at source on wages).

(B) Specified individuals

(i) In general

In the case of a recipient who is a specified individual, subparagraph (A) and paragraph (9) shall each be applied by substituting "to the extent that the expenses do not exceed the amount of the expenses which" for "to the extent that the expenses".

(ii) Specified individual

For purposes of clause (i), the term "specified individual" means any individual who—

(I) is subject to the requirements of section 16(a) of the Securities Exchange Act of 1934 with respect to the taxpayer or a related party to the taxpayer, or

(II) would be subject to such requirements if the taxpayer (or such related party) were an issuer of equity securities referred to in such section.

For purposes of this clause, a person is a related party with respect to another person if such person bears a relationship to such other person described in section 267(b) or 707(b).

(3) Reimbursed expenses

Expenses paid or incurred by the taxpayer, in connection with the performance by him of services for another person (whether or not such other person is his employer), under a reimbursement or other expense allowance arrangement with such other person, but this paragraph shall apply—

(A) where the services are performed for an employer, only if the employer has not treated such expenses in the manner provided in paragraph (2), or

(B) where the services are performed for a person other than an employer, only if the taxpayer accounts (to the extent provided by subsection (d)) to such person.

(4) Recreational, etc., expenses for employees

Expenses for recreational, social, or similar activities (including facilities therefor) primarily for the benefit of employees (other than employees who are highly compensated employees (within the meaning of section 414(q))). For purposes of this paragraph, an individual owning less than a 10-percent interest in the taxpayer's trade or business shall not be considered a shareholder or other owner, and for such purposes an individual shall be treated as owning any interest owned by a member of his family (within the meaning of section 267(c)(4)). This paragraph shall not apply for purposes of subsection (a)(3).

(5) Employees, stockholder, etc., business meetings

Expenses incurred by a taxpayer which are directly related to business meetings of his employees, stockholders, agents, or directors.

(6) Meetings of business leagues, etc.

Expenses directly related and necessary to attendance at a business meeting or convention of any organization described in section 501(c)(6) (relating to business leagues, chambers of commerce, real estate boards, and boards of trade) and exempt from taxation under section 501(a).

(7) Items available to public

Expenses for goods, services, and facilities made available by the taxpayer to the general public.

(8) Entertainment sold to customers

Expenses for goods or services (including the use of facilities) which are sold by the taxpayer in a bona fide transaction for an adequate and full consideration in money or money's worth.

(9) Expenses includible in income of persons who are not employees

Expenses paid or incurred by the taxpayer for goods, services, and facilities to the extent that the expenses are includible in the gross income of a recipient of the entertainment, amusement, or recreation who is not an em-

ployee of the taxpayer as compensation for services rendered or as a prize or award under section 74. The preceding sentence shall not apply to any amount paid or incurred by the taxpayer if such amount is required to be included (or would be so required except that the amount is less than \$600) in any information return filed by such taxpayer under part III of subchapter A of chapter 61 and is not so included.

For purposes of this subsection, any item referred to in subsection (a) shall be treated as an expense.

(f) Interest, taxes, casualty losses, etc.

This section shall not apply to any deduction allowable to the taxpayer without regard to its connection with his trade or business (or with his income-producing activity). In the case of a taxpayer which is not an individual, the preceding sentence shall be applied as if it were an individual.

(g) Treatment of entertainment, etc., type facility

For purposes of this chapter, if deductions are disallowed under subsection (a) with respect to any portion of a facility, such portion shall be treated as an asset which is used for personal, living, and family purposes (and not as an asset used in the trade or business).

(h) Attendance at conventions, etc.

(1) In general

In the case of any individual who attends a convention, seminar, or similar meeting which is held outside the North American area, no deduction shall be allowed under section 162 for expenses allocable to such meeting unless the taxpayer establishes that the meeting is directly related to the active conduct of his trade or business and that, after taking into account in the manner provided by regulations prescribed by the Secretary—

(A) the purpose of such meeting and the activities taking place at such meeting,

(B) the purposes and activities of the sponsoring organizations or groups,

(C) the residences of the active members of the sponsoring organization and the places at which other meetings of the sponsoring organization or groups have been held or will be held, and

(D) such other relevant factors as the taxpayer may present,

it is as reasonable for the meeting to be held outside the North American area as within the North American area.

(2) Conventions on cruise ships

In the case of any individual who attends a convention, seminar, or other meeting which is held on any cruise ship, no deduction shall be allowed under section 162 for expenses allocable to such meeting, unless the taxpayer meets the requirements of paragraph (5) and establishes that the meeting is directly related to the active conduct of his trade or business and that—

(A) the cruise ship is a vessel registered in the United States; and

(B) all ports of call of such cruise ship are located in the United States or in possessions of the United States.

With respect to cruises beginning in any calendar year, not more than \$2,000 of the expenses attributable to an individual attending one or more meetings may be taken into account under section 162 by reason of the preceding sentence.

(3) Definitions

For purposes of this subsection—

(A) North American area

The term “North American area” means the United States, its possessions, and the Trust Territory of the Pacific Islands, and Canada and Mexico.

(B) Cruise ship

The term “cruise ship” means any vessel sailing within or without the territorial waters of the United States.

(4) Subsection to apply to employer as well as to traveler

(A) Except as provided in subparagraph (B), this subsection shall apply to deductions otherwise allowable under section 162 to any person, whether or not such person is the individual attending the convention, seminar, or similar meeting.

(B) This subsection shall not deny a deduction to any person other than the individual attending the convention, seminar, or similar meeting with respect to any amount paid by such person to or on behalf of such individual if includible in the gross income of such individual. The preceding sentence shall not apply if the amount is required to be included in any information return filed by such person under part III of subchapter A of chapter 61 and is not so included.

(5) Reporting requirements

No deduction shall be allowed under section 162 for expenses allocable to attendance at a convention, seminar, or similar meeting on any cruise ship unless the taxpayer claiming the deduction attaches to the return of tax on which the deduction is claimed—

(A) a written statement signed by the individual attending the meeting which includes—

(i) information with respect to the total days of the trip, excluding the days of transportation to and from the cruise ship port, and the number of hours of each day of the trip which such individual devoted to scheduled business activities,

(ii) a program of the scheduled business activities of the meeting, and

(iii) such other information as may be required in regulations prescribed by the Secretary; and

(B) a written statement signed by an officer of the organization or group sponsoring the meeting which includes—

(i) a schedule of the business activities of each day of the meeting,

(ii) the number of hours which the individual attending the meeting attended such scheduled business activities, and

(iii) such other information as may be required in regulations prescribed by the Secretary.

(6) Treatment of conventions in certain Caribbean countries**(A) In general**

For purposes of this subsection, the term “North American area” includes, with respect to any convention, seminar, or similar meeting, any beneficiary country if (as of the time such meeting begins)—

(i) there is in effect a bilateral or multilateral agreement described in subparagraph (C) between such country and the United States providing for the exchange of information between the United States and such country, and

(ii) there is not in effect a finding by the Secretary that the tax laws of such country discriminate against conventions held in the United States.

(B) Beneficiary country

For purposes of this paragraph, the term “beneficiary country” has the meaning given to such term by section 212(a)(1)(A) of the Caribbean Basin Economic Recovery Act; except that such term shall include Bermuda.

(C) Authority to conclude exchange of information agreements**(i) In general**

The Secretary is authorized to negotiate and conclude an agreement for the exchange of information with any beneficiary country. Except as provided in clause (ii), an exchange of information agreement shall provide for the exchange of such information (not limited to information concerning nationals or residents of the United States or the beneficiary country) as may be necessary or appropriate to carry out and enforce the tax laws of the United States and the beneficiary country (whether criminal or civil proceedings), including information which may otherwise be subject to nondisclosure provisions of the local law of the beneficiary country such as provisions respecting bank secrecy and bearer shares. The exchange of information agreement shall be terminable by either country on reasonable notice and shall provide that information received by either country will be disclosed only to persons or authorities (including courts and administrative bodies) involved in the administration or oversight of, or in the determination of appeals in respect of, taxes of the United States or the beneficiary country and will be used by such persons or authorities only for such purposes.

(ii) Nondisclosure of qualified confidential information sought for civil tax purposes

An exchange of information agreement need not provide for the exchange of qualified confidential information which is sought only for civil tax purposes if—

(I) the Secretary of the Treasury, after making all reasonable efforts to negotiate an agreement which includes the

exchange of such information, determines that such an agreement cannot be negotiated but that the agreement which was negotiated will significantly assist in the administration and enforcement of the tax laws of the United States, and

(II) the President determines that the agreement as negotiated is in the national security interest of the United States.

(iii) Qualified confidential information defined

For purposes of this subparagraph, the term “qualified confidential information” means information which is subject to the nondisclosure provisions of any local law of the beneficiary country regarding bank secrecy or ownership of bearer shares.

(iv) Civil tax purposes

For purposes of this subparagraph, the determination of whether information is sought only for civil tax purposes shall be made by the requesting party.

(D) Coordination with other provisions

Any exchange of information agreement negotiated under subparagraph (C) shall be treated as an income tax convention for purposes of section 6103(k)(4). The Secretary may exercise his authority under subchapter A of chapter 78 to carry out any obligation of the United States under an agreement referred to in subparagraph (C).

(E) Determinations published in the Federal Register

The following shall be published in the Federal Register—

(i) any determination by the President under subparagraph (C)(ii) (including the reasons for such determination),

(ii) any determination by the Secretary under subparagraph (C)(ii) (including the reasons for such determination), and

(iii) any finding by the Secretary under subparagraph (A)(ii) (and any termination thereof).

(7) Seminars, etc. for section 212 purposes

No deduction shall be allowed under section 212 for expenses allocable to a convention, seminar, or similar meeting.

(i) Qualified nonpersonal use vehicle

For purposes of subsection (d), the term “qualified nonpersonal use vehicle” means any vehicle which, by reason of its nature, is not likely to be used more than a de minimis amount for personal purposes.

(j) Employee achievement awards**(1) General rule**

No deduction shall be allowed under section 162 or section 212 for the cost of an employee achievement award except to the extent that such cost does not exceed the deduction limitations of paragraph (2).

(2) Deduction limitations

The deduction for the cost of an employee achievement award made by an employer to an employee—

(A) which is not a qualified plan award, when added to the cost to the employer for all other employee achievement awards made to such employee during the taxable year which are not qualified plan awards, shall not exceed \$400, and

(B) which is a qualified plan award, when added to the cost to the employer for all other employee achievement awards made to such employee during the taxable year (including employee achievement awards which are not qualified plan awards), shall not exceed \$1,600.

(3) Definitions

For purposes of this subsection—

(A) Employee achievement award

The term “employee achievement award” means an item of tangible personal property which is—

(i) transferred by an employer to an employee for length of service achievement or safety achievement,

(ii) awarded as part of a meaningful presentation, and

(iii) awarded under conditions and circumstances that do not create a significant likelihood of the payment of disguised compensation.

(B) Qualified plan award

(i) In general

The term “qualified plan award” means an employee achievement award awarded as part of an established written plan or program of the taxpayer which does not discriminate in favor of highly compensated employees (within the meaning of section 414(q)) as to eligibility or benefits.

(ii) Limitation

An employee achievement award shall not be treated as a qualified plan award for any taxable year if the average cost of all employee achievement awards which are provided by the employer during the year, and which would be qualified plan awards but for this subparagraph, exceeds \$400. For purposes of the preceding sentence, average cost shall be determined by including the entire cost of qualified plan awards, without taking into account employee achievement awards of nominal value.

(4) Special rules

For purposes of this subsection—

(A) Partnerships

In the case of an employee achievement award made by a partnership, the deduction limitations contained in paragraph (2) shall apply to the partnership as well as to each member thereof.

(B) Length of service awards

An item shall not be treated as having been provided for length of service achievement if the item is received during the recipient’s 1st 5 years of employment or if the recipient received a length of service

achievement award (other than an award excludable under section 132(e)(1)) during that year or any of the prior 4 years.

(C) Safety achievement awards

An item provided by an employer to an employee shall not be treated as having been provided for safety achievement if—

(i) during the taxable year, employee achievement awards (other than awards excludable under section 132(e)(1)) for safety achievement have previously been awarded by the employer to more than 10 percent of the employees of the employer (excluding employees described in clause (ii)), or

(ii) such item is awarded to a manager, administrator, clerical employee, or other professional employee.

(k) Business meals

(1) In general

No deduction shall be allowed under this chapter for the expense of any food or beverages unless—

(A) such expense is not lavish or extravagant under the circumstances, and

(B) the taxpayer (or an employee of the taxpayer) is present at the furnishing of such food or beverages.

(2) Exceptions

Paragraph (1) shall not apply to—

(A) any expense described in paragraph (2), (3), (4), (7), (8), or (9) of subsection (e), and

(B) any other expense to the extent provided in regulations.

(l) Additional limitations on entertainment tickets

(1) Entertainment tickets

(A) In general

In determining the amount allowable as a deduction under this chapter for any ticket for any activity or facility described in subsection (d)(2), the amount taken into account shall not exceed the face value of such ticket.

(B) Exception for certain charitable sports events

Subparagraph (A) shall not apply to any ticket for any sports event—

(i) which is organized for the primary purpose of benefiting an organization which is described in section 501(c)(3) and exempt from tax under section 501(a),

(ii) all of the net proceeds of which are contributed to such organization, and

(iii) which utilizes volunteers for substantially all of the work performed in carrying out such event.

(2) Skyboxes, etc.

In the case of a skybox or other private luxury box leased for more than 1 event, the amount allowable as a deduction under this chapter with respect to such events shall not exceed the sum of the face value of non-luxury box seat tickets for the seats in such box covered by the lease. For purposes of the preceding sentence, 2 or more related leases shall be treated as 1 lease.

(m) Additional limitations on travel expenses

(1) Luxury water transportation

(A) In general

No deduction shall be allowed under this chapter for expenses incurred for transportation by water to the extent such expenses exceed twice the aggregate per diem amounts for days of such transportation. For purposes of the preceding sentence, the term “per diem amounts” means the highest amount generally allowable with respect to a day to employees of the executive branch of the Federal Government for per diem while away from home but serving in the United States.

(B) Exceptions

Subparagraph (A) shall not apply to—

- (i) any expense allocable to a convention, seminar, or other meeting which is held on any cruise ship, and
- (ii) any expense described in paragraph (2), (3), (4), (7), (8), or (9) of subsection (e).

(2) Travel as form of education

No deduction shall be allowed under this chapter for expenses for travel as a form of education.

(3) Travel expenses of spouse, dependent, or others

No deduction shall be allowed under this chapter (other than section 217) for travel expenses paid or incurred with respect to a spouse, dependent, or other individual accompanying the taxpayer (or an officer or employee of the taxpayer) on business travel, unless—

- (A) the spouse, dependent, or other individual is an employee of the taxpayer,
- (B) the travel of the spouse, dependent, or other individual is for a bona fide business purpose, and
- (C) such expenses would otherwise be deductible by the spouse, dependent, or other individual.

(n) Only 50 percent of meal and entertainment expenses allowed as deduction

(1) In general

The amount allowable as a deduction under this chapter for—

- (A) any expense for food or beverages, and
- (B) any item with respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation, or with respect to a facility used in connection with such activity,

shall not exceed 50 percent of the amount of such expense or item which would (but for this paragraph) be allowable as a deduction under this chapter.

(2) Exceptions

Paragraph (1) shall not apply to any expense if—

- (A) such expense is described in paragraph (2), (3), (4), (7), (8), or (9) of subsection (e),
- (B) in the case of an expense for food or beverages, such expense is excludable from the gross income of the recipient under sec-

tion 132 by reason of subsection (e) thereof (relating to de minimis fringes),

(C) such expense is covered by a package involving a ticket described in subsection (l)(1)(B),

(D) in the case of an employer who pays or reimburses moving expenses of an employee, such expenses are includible in the income of the employee under section 82, or

(E) such expense is for food or beverages—

(i) required by any Federal law to be provided to crew members of a commercial vessel,

(ii) provided to crew members of a commercial vessel—

(I) which is operating on the Great Lakes, the Saint Lawrence Seaway, or any inland waterway of the United States, and

(II) which is of a kind which would be required by Federal law to provide food and beverages to crew members if it were operated at sea,

(iii) provided on an oil or gas platform or drilling rig if the platform or rig is located offshore, or

(iv) provided on an oil or gas platform or drilling rig, or at a support camp which is in proximity and integral to such platform or rig, if the platform or rig is located in the United States north of 54 degrees north latitude.

Clauses (i) and (ii) of subparagraph (E) shall not apply to vessels primarily engaged in providing luxury water transportation (determined under the principles of subsection (m)). In the case of the employee, the exception of subparagraph (A) shall not apply to expenses described in subparagraph (D).

(3) Special rule for individuals subject to Federal hours of service

(A) In general

In the case of any expenses for food or beverages consumed while away from home (within the meaning of section 162(a)(2)) by an individual during, or incident to, the period of duty subject to the hours of service limitations of the Department of Transportation, paragraph (1) shall be applied by substituting “the applicable percentage” for “50 percent”.

(B) Applicable percentage

For purposes of this paragraph, the term “applicable percentage” means the percentage determined under the following table:

For taxable years beginning in calendar year—	The applicable percentage is—
1998 or 1999	55
2000 or 2001	60
2002 or 2003	65
2004 or 2005	70
2006 or 2007	75
2008 or thereafter	80.

(o) Regulatory authority

The Secretary shall prescribe such regulations as he may deem necessary to carry out the purposes of this section, including regulations pre-

scribing whether subsection (a) or subsection (b) applies in cases where both such subsections would otherwise apply.

(Added Pub. L. 87-834, §4(a)(1), Oct. 16, 1962, 76 Stat. 974; amended Pub. L. 88-272, title II, §217(a), Feb. 26, 1964, 78 Stat. 56; Pub. L. 94-455, title VI, §602(a), title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1572, 1834; Pub. L. 95-600, title III, §361(a), (b), title VII, §701(g)(1)-(3), Nov. 6, 1978, 92 Stat. 2847, 2903, 2904; Pub. L. 96-222, title I, §103(a)(10)(A), (B) Apr. 1, 1980, 94 Stat. 212; Pub. L. 96-598, §5(a), Dec. 24, 1980, 94 Stat. 3488; Pub. L. 96-605, title I, §108(a), Dec. 28, 1980, 94 Stat. 3524; Pub. L. 96-608, §4(a), Dec. 28, 1980, 94 Stat. 3552; Pub. L. 97-34, title II, §265(a), (b), Aug. 13, 1981, 95 Stat. 265; Pub. L. 97-248, title III, §§307(a)(1), 308(a), Sept. 3, 1982, 96 Stat. 589, 591; Pub. L. 97-424, title V, §543(a), Jan. 6, 1983, 96 Stat. 2195; Pub. L. 98-67, title I, §102(a), title II, §222(a), Aug. 5, 1983, 97 Stat. 369, 395; Pub. L. 98-369, div. A, title I, §179(b)(1), title VIII, §801(c), July 18, 1984, 98 Stat. 718, 995; Pub. L. 99-44, §§1(a), 2, 6(b), May 24, 1985, 99 Stat. 77, 79; Pub. L. 99-514, title I, §§122(c), (d), 142(a)-(c), title XI, §1114(b)(6), Oct. 22, 1986, 100 Stat. 2110, 2117-2120, 2451; Pub. L. 100-647, title I, §§1001(g)(1)-(4)(A), (5), 1018(u)(2), title VI, §6003(a), Nov. 10, 1988, 102 Stat. 3351, 3352, 3590, 3684; Pub. L. 101-239, title VII, §§7816(a), 7841(d)(18), Dec. 19, 1989, 103 Stat. 2420, 2429; Pub. L. 101-508, title XI, §11802(b), Nov. 5, 1990, 104 Stat. 1388-529; Pub. L. 103-66, title XIII, §§13209(a), (b), 13210(a), (b), 13272(a), Aug. 10, 1993, 107 Stat. 469, 542; Pub. L. 105-34, title IX, §969(a), Aug. 5, 1997, 111 Stat. 896; Pub. L. 108-357, title VIII, §907(a), Oct. 22, 2004, 118 Stat. 1654; Pub. L. 109-135, title IV, §403(mm), Dec. 21, 2005, 119 Stat. 2632.)

REFERENCES IN TEXT

Section 16 of the Securities Exchange Act of 1934, referred to in subsec. (e)(2)(B)(ii), is classified to section 78p of Title 15, Commerce and Trade.

Section 212(a)(1)(A) of the Caribbean Basin Economic Recovery Act, referred to in subsec. (h)(6)(B), is classified to section 2702(a)(1)(A) of Title 19, Customs Duties.

AMENDMENTS

2005—Subsec. (e)(2)(B)(ii). Pub. L. 109-135, §403(mm)(1), (2), inserted “or a related party to the taxpayer” after “with respect to the taxpayer” in subcl. (I), “(or such related party)” after “the taxpayer” in subcl. (II), and “For purposes of this clause, a person is a related party with respect to another person if such person bears a relationship to such other person described in section 267(b) or 707(b).” at end.

2004—Subsec. (e)(2). Pub. L. 108-357 reenacted heading without change and amended text generally. Prior to amendment, text read as follows: “Expenses for goods, services, and facilities, to the extent that the expenses are treated by the taxpayer, with respect to the recipient of the entertainment, amusement, or recreation, as compensation to an employee on the taxpayer’s return of tax under this chapter and as wages to such employee for purposes of chapter 24 (relating to withholding of income tax at source on wages).”

1997—Subsec. (n)(3). Pub. L. 105-34 added par. (3).

1993—Subsec. (a)(3). Pub. L. 103-66, §13210(a), added par. (3).

Subsec. (e)(4). Pub. L. 103-66, §13210(b), inserted at end “This paragraph shall not apply for purposes of subsection (a)(3).”

Subsec. (m)(3). Pub. L. 103-66, §13272(a), added par. (3).

Subsec. (n). Pub. L. 103-66, §13209(a), (b), substituted “50” for “80” in heading and in concluding provisions of par. (1).

1990—Subsec. (l)(2). Pub. L. 101-508, §11802(b)(1), in amending par. (2) generally, struck out “(A) In general” and subpar. (B) which provided for phase-in deductions of skybox tickets in the 1987 and 1988 taxable years.

Subsec. (n)(2). Pub. L. 101-508, §11802(b)(2)(A)(ii), (iii), substituted “described in subparagraph (D)” for “described in subparagraph (E)” and “of subparagraph (E)” for “of subparagraph (F)” in concluding provisions.

Subsec. (n)(2)(D) to (F). Pub. L. 101-508, §11802(b)(2)(A)(i), redesignated subpars. (E) and (F) as (D) and (E), respectively, and struck out former subpar. (D) which read as follows: “in the case of an expense for food or beverages before January 1, 1989, such expense is an integral part of a qualified meeting.”

Subsec. (n)(3). Pub. L. 101-508, §11802(b)(2)(B), struck out par. (3) “Qualified meeting” which read as follows: “For purposes of paragraph (2)(D), the term ‘qualified meeting’ means any convention, seminar, annual meeting, or similar business program with respect to which—

“(A) an expense for food or beverages is not separately stated,

“(B) more than 50 percent of the participants are away from home,

“(C) at least 40 individuals attend, and

“(D) such food and beverages are part of a program which includes a speaker.”

1989—Subsec. (n)(2). Pub. L. 101-239, §7816(a), added a new subpar. (E), substantially identical to former subpar. (E), and moved sentence formerly appearing between subpars. (E) and (F) to end of concluding provisions after subpar. (F).

Subsec. (n)(2)(F)(i). Pub. L. 101-239, §7841(d)(18), inserted “any” before “Federal law”.

1988—Subsec. (b)(1). Pub. L. 100-647, §1018(u)(2), related to execution of amendment by Pub. L. 99-514, §122(c)(2), see 1986 Amendment note below.

Subsec. (h)(1), (2). Pub. L. 100-647, §1001(g)(5), substituted “trade or business and that” for “trade or business that”.

Subsec. (k)(2). Pub. L. 100-647, §1001(g)(2), amended par. (2) generally. Prior to amendment, par. (2) read as follows: “Paragraph (1) shall not apply to any expense if subsection (a) does not apply to such expense by reason of paragraph (2), (3), (4), (7), (8), or (9) of subsection (e).”

Subsec. (m)(1)(B)(ii). Pub. L. 100-647, §1001(g)(3), amended cl. (ii) generally. Prior to amendment, cl. (ii) read as follows: “any expense to which subsection (a) does not apply by reason of paragraph (2), (3), (4), (7), (8), or (9) of subsection (e).”

Subsec. (n)(2). Pub. L. 100-647, §6003(a), struck out “or” at end of subpar. (D), substituted “, or” for the period at end of subpar. (E), and added subpar. (F) and flush sentence at end.

Pub. L. 100-647, §1001(g)(4)(A), struck out “or” at end of subpar. (C), substituted “, or” for the period at end of subpar. (D), and added subpar. (E) and flush sentence at end.

Pub. L. 100-647, §1001(g)(1), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: “subsection (a) does not apply to such expense by reason of paragraph (2), (3), (4), (7), (8), or (9) of subsection (e).”

1986—Subsec. (b)(1). Pub. L. 99-514, §122(c)(1)-(3), and Pub. L. 100-647, §1018(u)(2), made conforming amendments to subpars. (A) and (B) and struck out subpar. (C) which read as follows: “an item of tangible personal property which is awarded to an employee by reason of length of service, productivity, or safety achievement, but only to the extent that—

“(i) the cost of such item to the taxpayer does not exceed \$400, or

“(ii) such item is a qualified plan award.”

Subsec. (b)(3). Pub. L. 99-514, §122(c)(4), struck out par. (3) relating to qualified plan award, defining such term in subpar. (A), and providing for average amount of awards in subpar. (B) and maximum amount per item in subpar. (C).

Subsec. (e)(1). Pub. L. 99-514, §142(a)(2)(A), redesignated par. (2) as (1) and struck out former par. (1), business meals, which read as follows: “Expenses for food and beverages furnished to any individual under circumstances which (taking into account the surroundings in which furnished, the taxpayer’s trade, business, or income-producing activity and the relationship to such trade, business, or activity of the persons to whom the food and beverages are furnished) are of a type generally considered to be conducive to a business discussion.”

Subsec. (e)(2). Pub. L. 99-514, §142(a)(2)(A), redesignated par. (3) as (2). Former par. (2) redesignated (1).

Subsec. (e)(3). Pub. L. 99-514, §142(a)(2), redesignated par. (4) as (3) and substituted “paragraph (2)” for “paragraph (3)” in subpar. (A). Former par. (3) redesignated (2).

Subsec. (e)(4). Pub. L. 99-514, §1114(b)(6), which directed the substitution of “highly compensated employees (within the meaning of section 414(q))” for “officers, shareholders or other owners, or highly compensated employees” in par. (5) was executed to par. (4) to reflect the probable intent of Congress, in view of the redesignation of par. (5) as (4) by section 142(a)(2)(A) of Pub. L. 99-514.

Pub. L. 99-514, §142(a)(2)(A), redesignated par. (5) as (4). Former par. (4) redesignated (3).

Subsec. (e)(5) to (10). Pub. L. 99-514, §142(a)(2)(A), redesignated pars. (5) to (10) as pars. (4) to (9), respectively.

Subsec. (h). Pub. L. 99-514, §142(c), struck out “or 212” after “section 162” in introductory provisions of pars. (1), (2), and (5), in closing provisions of par. (2), and in par. (4)(A), struck out “or to an activity described in section 212 and” after “active conduct of his trade or business” in introductory provisions of pars. (1) and (2), and added par. (7).

Subsec. (j). Pub. L. 99-514, §122(d), added subsec. (j). Former subsec. (j) redesignated (k).

Subsec. (k). Pub. L. 99-514, §142(a)(1), added subsec. (k). Former subsec. (k) redesignated (o).

Subsecs. (l) to (n). Pub. L. 99-514, §142(b), added subsecs. (l) to (n).

Subsec. (o). Pub. L. 99-514, §142(a)(1), redesignated former subsec. (k) as (o).

1985—Subsec. (d). Pub. L. 99-44, §2(a), inserted at end “This subsection shall not apply to any qualified non-personal use vehicle (as defined in subsection (i)).”

Pub. L. 99-44, §1(a), substituted “adequate records or by sufficient evidence corroborating the taxpayer’s own statement” for “adequate contemporaneous records”, and provided that the Internal Revenue Code of 1954 [now 1986] [this title] shall be applied as if “contemporaneous” had not been added to subsec. (d). See Effective Date of 1985 Amendment note below.

Subsecs. (i), (j). Pub. L. 99-44, §2(b), added subsec. (i) and redesignated former subsec. (i) as (j).

1984—Subsec. (d). Pub. L. 98-369, §179(b), substituted, in introductory provisions, “No deduction or credit” for “No deduction” and, in provisions following par. (4), “adequate contemporaneous records” for “adequate records or by sufficient evidence corroborating his own statement” and “the facility or property” for “the facility” in two places, and added par. (4).

Subsec. (h)(6)(D). Pub. L. 98-369, §801(c), substituted in heading “with other provisions” for “with section 6103” and in text inserted provision that the Secretary may exercise his authority under subchapter A of chapter 78 to carry out any obligations of the United States under an agreement referred to in subpar. (C).

1983—Subsec. (e)(3). Pub. L. 98-67, §102(a), repealed amendments made by Pub. L. 97-248. See 1982 Amendment note below.

Subsec. (h)(2). Pub. L. 97-424, §543(a)(1), inserted provisions relating to requirements of par. (5) and the description in section 212, and inserted the \$2,000 limit relating to section 162 or 212.

Subsec. (h)(5). Pub. L. 97-424, §543(a)(2), added par. (5).

Subsec. (h)(6). Pub. L. 98-67, §227(a), added par. (6).

1982—Subsec. (e)(3). Pub. L. 97-248 provided that, applicable to payments of interest, dividends, and patron-

age dividends paid or credited after June 30, 1983, par. (3) is amended by inserting “subchapter A of” before “chapter 24”. Section 102(a), (b) of Pub. L. 98-67, title I, Aug. 5, 1983, 97 Stat. 369, repealed subtitle A (§§301-308) of title III of Pub. L. 97-248 as of the close of June 30, 1983, and provided that the Internal Revenue Code of 1954 [now 1986] [this title] shall be applied and administered (subject to certain exceptions) as if such subtitle A (and the amendments made by such subtitle A) had not been enacted.

1981—Subsec. (b)(1)(C). Pub. L. 97-34, §265(a), excluded from term “gift” an award for productivity, designated existing provisions as cl. (i), and as so designated, increased the limitation to \$400 from \$100, and added cl. (ii).

Subsec. (b)(3). Pub. L. 97-34, §265(b), added par. (3).

1980—Subsec. (a)(2)(C). Pub. L. 96-222, §103(a)(10)(A), struck out “country” after “the case of a”.

Subsec. (e)(10). Pub. L. 96-605 and Pub. L. 96-598 made identical amendments by adding par. (10).

Subsec. (h) Pub. L. 96-608 substituted provision disallowing any deductions for expenses allocable to a convention, seminar, or other similar meeting outside the North American area unless, taking certain factors into account, it is as reasonable for the meeting to be held outside the North American area as within it, disallowing any deductions for a convention, seminar, or similar meeting held on any cruise ship, and defining North American area and cruise ship, for provision allowing deductions with respect to not more than 2 foreign conventions per year, limiting deductible transportation cost to not to exceed the cost of coach or economy air fare, permitting transportation costs to be fully deductible only if at least one-half of the days are devoted to business related activities, disallowing deductions for subsistence expenses unless the individual attends two-thirds of the business activities, limiting deductible subsistence costs to not to exceed the per diem rate for United States civil servants, defining foreign convention and subsistence expenses, providing that if transportation expenses or subsistence expenses are not separately stated or do not reflect the proper allocation all amounts paid be treated as subsistence expenses, and prescribing special reporting and substantiation requirements.

1978—Subsec. (a)(1). Pub. L. 95-600, §361(a), substituted provisions allowing no deduction for expenses paid or incurred with respect to a facility which is used in conjunction with an activity which is of a type generally considered to constitute entertainment, amusement, or recreation for provisions allowing a deduction for expenses paid or incurred with respect to a facility if the facility used is primarily for the furtherance of the taxpayer’s business, and the expense is “directly related” to the active conduct of taxpayer’s business.

Subsec. (a)(2)(C). Pub. L. 95-600, §361(b), as amended by Pub. L. 96-222, §103(a)(10)(B), added subpar. (C).

Subsec. (h)(3). Pub. L. 95-600, §701(g)(3), substituted “at least one-half” for “more than one-half” in first sentence.

Subsec. (h)(6)(D). Pub. L. 95-600, §701(g)(1), designated existing provisions as cl. (i), inserted introductory phrase “Except as provided in clause (ii)” and substituted “For the purposes” for “For purpose”, and added cl. (ii).

Subsec. (h)(6)(E). Pub. L. 95-600, §701(g)(2), added subpar. (E).

1976—Subsecs. (c)(1), (d). Pub. L. 94-455, §1906(b)(13)(A), struck out “or his delegate” after “Secretary”.

Subsec. (h). Pub. L. 94-455, §602(a), added subsec. (h). Former subsec. (h) redesignated (i).

Subsec. (i). Pub. L. 94-455, §§602(a), 1906(b)(13)(A), redesignated former subsec. (h) as (i) and struck out “or his delegate” after “Secretary”.

1964—Subsec. (c). Pub. L. 88-272 limited subsec. (c) to individuals traveling outside the United States.

EFFECTIVE DATE OF 2005 AMENDMENT

Amendments by Pub. L. 109-135 effective as if included in the provisions of the American Jobs Creation

Act of 2004, Pub. L. 108-357, to which they relate, see section 403(nn) of Pub. L. 109-135, set out as a note under section 26 of this title.

EFFECTIVE DATE OF 2004 AMENDMENT

Pub. L. 108-357, title VIII, §907(b), Oct. 22, 2004, 118 Stat. 1655, provided that: "The amendment made by this section [amending this section] shall apply to expenses incurred after the date of the enactment of this Act [Oct. 22, 2004]."

EFFECTIVE DATE OF 1997 AMENDMENT

Section 969(b) of Pub. L. 105-34 provided that: "The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1997."

EFFECTIVE DATE OF 1993 AMENDMENT

Section 13209(c) of Pub. L. 103-66 provided that: "The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1993."

Section 13210(c) of Pub. L. 103-66 provided that: "The amendments made by this section [amending this section] shall apply to amounts paid or incurred after December 31, 1993."

Section 13272(b) of Pub. L. 103-66 provided that: "The amendment made by this section [amending this section] shall apply to amounts paid or incurred after December 31, 1993."

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by section 7816(a) of Pub. L. 101-239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100-647, to which such amendment relates, see section 7817 of Pub. L. 101-239, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1001(g)(1)-(4)(A), (5) of Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

Section 6003(b) of Pub. L. 100-647 provided that: "(1) Clauses (i) and (ii) of section 274(n)(2)(F) of the 1986 Code, as added by subsection (a), shall apply to taxable years beginning after December 31, 1988.

"(2) Clauses (iii) and (iv) of section 274(n)(2)(F) of the 1986 Code, as added by subsection (a), shall apply to taxable years beginning after December 31, 1987."

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 122(c), (d) of Pub. L. 99-514 applicable to prizes and awards granted after Dec. 31, 1986, see section 151(c) of Pub. L. 99-514, set out as a note under section 1 of this title.

Amendment by section 142(a)-(c) of Pub. L. 99-514 applicable to taxable years beginning after Dec. 31, 1986, see section 151(a) of Pub. L. 99-514, set out as a note under section 1 of this title.

Amendment by section 1114(b)(6) of Pub. L. 99-514 applicable to years beginning after Dec. 31, 1986, see section 1114(c)(1) of Pub. L. 99-514, set out as a note under section 414 of this title.

EFFECTIVE DATE OF 1985 AMENDMENT

Section 6(a)-(c) of Pub. L. 99-44, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that: "(a) REPEALS.—The amendment and repeals made by subsections (a) and (b) of section 1 [amending this section and repealing section 179(b)(2), (3) of Pub. L. 98-369 which had amended sections 6653 and 6695 of this title] shall take effect as if included in the amendments made by section 179(b) of the Tax Reform Act of 1984 [Pub. L. 98-369].

"(b) RESTORATION OF PRIOR LAW FOR 1985.—For taxable years beginning in 1985, section 274(d) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] shall apply as it read before the amendments made by section 179(b)(1) of the Tax Reform Act of 1984 [Pub. L. 98-369, see 1984 Amendments note above].

"(c) EXCEPTION FROM SUBSTANTIATION REQUIREMENTS FOR QUALIFIED NONPERSONAL USE VEHICLES.—The amendments made by section 2 [amending this section] shall apply to taxable years beginning after December 31, 1985."

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 179(b)(1) of Pub. L. 98-369 applicable to taxable years beginning after Dec. 31, 1984, see section 179(d)(2) of Pub. L. 98-369, set out as an Effective Date note under section 280F of this title.

Amendment by section 801(c) of Pub. L. 98-369 applicable to transactions after Dec. 31, 1984, in taxable years ending after such date, see section 805(a)(1) of Pub. L. 98-369, as amended, set out as a note under section 245 of this title.

EFFECTIVE DATE OF 1983 AMENDMENTS

Section 222(b) of Pub. L. 98-67 provided that: "The amendment made by subsection (a) [amending this section] shall apply to conventions, seminars, or other meetings which begin after June 30, 1983."

Section 543(b) of Pub. L. 97-424 provided that: "The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1982."

EFFECTIVE DATE OF 1981 AMENDMENT

Section 265(c) of Pub. L. 97-34 provided that: "The amendments made by this section [amending this section] shall apply to taxable years ending on or after the date of the enactment of this Act [Aug. 13, 1981]."

EFFECTIVE DATE OF 1980 AMENDMENTS

Section 4(b) of Pub. L. 96-608, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that: "The amendment made by subsection (a) of this section [amending this section] shall apply to conventions, seminars, and meetings beginning after December 31, 1980, except that in the case of any convention, seminar, or meeting beginning after such date which was scheduled on or before such date, a person, in such manner as the Secretary of the Treasury or his delegate may prescribe, may elect to have the provisions of section 274(h) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] be applied to such convention seminar or meeting without regard to such amendment."

Section 5(b) of Pub. L. 96-598 and section 108(b) of Pub. L. 96-605 provided that: "The amendment made by this section [amending this section] shall apply to any expenses paid or incurred after December 31, 1980, in taxable years ending after such date."

Amendment by Pub. L. 96-222 effective, except as otherwise provided, as if it had been included in the provisions of the Revenue Act of 1978, Pub. L. 95-600, to which such amendment relates, see section 201 of Pub. L. 96-222, set out as a note under section 32 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Section 361(c) of Pub. L. 95-600 provided that: "The amendments made by this section [amending this section] shall apply to items paid or incurred after December 31, 1978, in taxable years ending after such date."

Section 701(g)(4) of Pub. L. 95-600 provided that: "The amendments made by this subsection [amending this section] shall apply to conventions beginning after December 31, 1976."

EFFECTIVE DATE OF 1976 AMENDMENT

Section 602(b) of Pub. L. 94-455 provided that: "The amendments made by this section [amending this section] shall apply to conventions beginning after December 31, 1976."

EFFECTIVE DATE OF 1964 AMENDMENT

Section 217(b) of Pub. L. 88-272 provided that: "The amendment made by subsection (a) [amending this section] shall apply with respect to taxable years ending after December 31, 1962, but only in respect of periods after such date."

EFFECTIVE DATE

Section applicable with respect to taxable years ending after Dec. 31, 1962, but only in respect of periods after such date, see section 4(c) of Pub. L. 87-834, set out as an Effective Date of 1962 Amendment note under section 162 of this title.

REGULATIONS

Secretary of the Treasury or his delegate to issue before Feb. 1, 1983, final regulations to carry out amendments made by section 1114 of Pub. L. 99-514, see section 1141 of Pub. L. 99-514, set out as a note under section 401 of this title.

Section 5 of Pub. L. 99-44 provided that: "Not later than October 1, 1985, the Secretary of the Treasury or his delegate shall prescribe regulations to carry out the provisions of this Act [amending sections 274, 280F, 3402, 6653, and 6695 of this title, and enacting provisions set out as notes under sections 274, 280F, 3402, and 6653 of this title] which shall fully reflect such provisions."

Section 1(c) of Pub. L. 99-44 provided that: "Regulations issued before the date of the enactment of this Act [May 24, 1985] to carry out the amendments made by paragraphs (1)(C), (2), and (3) of section 179(b) of the Tax Reform Act of 1984 [Pub. L. 98-369, amending sections 274, 6653, and 6695 of this title] shall have no force and effect."

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101-508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101-508, set out as a note under section 45K of this title.

TERMINATION OF TRUST TERRITORY OF THE PACIFIC ISLANDS

For termination of Trust Territory of the Pacific Islands, see note set out preceding section 1681 of Title 48, Territories and Insular Possessions.

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101-1147 and 1171-1177] or title XVIII [§§ 1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

CERTAIN RECORDKEEPING REQUIREMENTS

For treatment of use of automobile by I.R.S. special agent for purposes of this section and section 132 of this title, see section 1567 of Pub. L. 99-514, set out as a note under section 132 of this title.

SUBSTANTIATION BY ADEQUATE CONTEMPORANEOUS RECORDS

Section 1(a) of Pub. L. 99-44, as amended by Pub. L. 99-514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided in part that: "the Internal Revenue Code of 1986 [formerly I.R.C. 1954] shall be applied and administered as if the word 'contemporaneous' had not been added [by Pub. L. 98-369] to such subsection (d) [subsec. (d) of this section]."

USE OF FACILITIES IN CASE OF INDEPENDENT CONTRACTORS, ETC.

Section 103(a)(10)(C) of Pub. L. 96-222, as amended by Pub. L. 99-514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

"(i) IN GENERAL.—Subsection (a) of section 274 of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] (relating to disallowance of certain entertainment, etc., expenses) shall not apply to expenses paid or incurred by the taxpayer for goods, services, and facilities to the extent that the expenses are includible in the gross income of a recipient of the entertainment, amusement, or recreation who is not an employee of the taxpayer as compensation for services rendered or as a prize or award under section 74 of such Code.

"(ii) INFORMATION RETURN REQUIREMENT.—Clause (i) shall not apply to any amount paid or incurred by the taxpayer if such amount is required to be included in any information return filed by such taxpayer under part III of subchapter A of chapter 61 of such Code [section 6031 et seq. of this title] and is not so included.

"(iii) APPLICATION OF SUBPARAGRAPH.—This subparagraph shall only apply with respect to expenses paid or incurred during 1979 or 1980."

§ 275. Certain taxes

(a) General rule

No deduction shall be allowed for the following taxes:

(1) Federal income taxes, including—

(A) the tax imposed by section 3101 (relating to the tax on employees under the Federal Insurance Contributions Act);

(B) the taxes imposed by sections 3201 and 3211 (relating to the taxes on railroad employees and railroad employee representatives); and

(C) the tax withheld at source on wages under section 3402.

(2) Federal war profits and excess profits taxes.

(3) Estate, inheritance, legacy, succession, and gift taxes.

(4) Income, war profits, and excess profits taxes imposed by the authority of any foreign country or possession of the United States if the taxpayer chooses to take to any extent the benefits of section 901.

(5) Taxes on real property, to the extent that section 164(d) requires such taxes to be treated as imposed on another taxpayer.

(6) Taxes imposed by chapters 41, 42, 43, 44, 45, 46, and 54.

Paragraph (1) shall not apply to the tax imposed by section 59A. Paragraph (1) shall not apply to any taxes to the extent such taxes are allowable as a deduction under section 164(f).

(b) Cross reference

For disallowance of certain other taxes, see section 164(c).

(Added Pub. L. 88-272, title II, § 207(b)(3)(A), Feb. 26, 1964, 78 Stat. 42; amended Pub. L. 93-406, title II, § 1016(a)(1), Sept. 2, 1974, 88 Stat. 929; Pub. L. 94-455, title XIII, § 1307(d)(2)(A), title XVI, § 1605(b)(1), title XIX, § 1901(a)(39), Oct. 4, 1976, 90 Stat. 1727, 1754, 1771; Pub. L. 95-600, title VII, § 701(t)(3)(B), Nov. 6, 1978, 92 Stat. 2912; Pub. L. 97-248, title III, § 305(a), 308(a), Sept. 3, 1982, 96 Stat. 588, 591; Pub. L. 98-21, title I, § 124(c)(5), Apr. 20, 1983, 97 Stat. 91; Pub. L. 98-67, title I, § 102(a) Aug. 5, 1983, 97 Stat. 369; Pub. L. 98-369,

div. A, title I, § 67(b)(2), title VIII, § 801(d)(5), July 18, 1984, 98 Stat. 587, 996; Pub. L. 99-499, title V, § 516(b)(2)(B), Oct. 17, 1986, 100 Stat. 1771; Pub. L. 100-203, title X, § 10228(b), Dec. 22, 1987, 101 Stat. 1330-418; Pub. L. 106-519, § 4(2), Nov. 15, 2000, 114 Stat. 2432; Pub. L. 108-357, title I, § 101(b)(5), title VIII, § 802(b)(1), Oct. 22, 2004, 118 Stat. 1423, 1568; Pub. L. 110-172, § 11(g)(5), Dec. 29, 2007, 121 Stat. 2490.)

REFERENCES IN TEXT

The Federal Insurance Contributions Act, referred to in subsec. (a)(1)(A), is act Aug. 16, 1954, ch. 736, §§ 3101, 3102, 3111, 3112, 3121 to 3128, 68A Stat. 415, as amended, which is classified generally to chapter 21 (§ 3101 et seq.) of this title. For complete classification of this Act to the Code, see section 3128 of this title and Tables.

CODIFICATION

Pub. L. 95-600, § 701(t)(3)(B) (effective Oct. 4, 1976, see Pub. L. 95-600, § 701(t)(5), set out as an Effective Date of 1978 Amendment note under section 859 of this title) repealed § 1605(b)(1) of Pub. L. 94-455, cited as a credit to this section, which had duplicated the amendment to subsec. (a)(6) made by § 1307(d)(2)(A) of Pub. L. 94-455.

AMENDMENTS

2007—Subsec. (a)(4). Pub. L. 110-172 substituted “if the taxpayer chooses to take to any extent the benefits of section 901.” for “if—

“(A) the taxpayer chooses to take to any extent the benefits of section 901, or

“(B) such taxes are paid or accrued with respect to foreign trade income (within the meaning of section 923(b)) of a FSC.”

2004—Subsec. (a). Pub. L. 108-357, § 101(b)(5)(B), struck out at end of concluding provisions “A rule similar to the rule of section 943(d) shall apply for purposes of paragraph (4)(C).”

Subsec. (a)(4). Pub. L. 108-357, § 101(b)(5)(A), inserted “or” at end of subpar. (A), substituted period for “or” at end of subpar. (B), and struck out subpar. (C) which read as follows: “such taxes are paid or accrued with respect to qualifying foreign trade income (as defined in section 941).”

Subsec. (a)(6). Pub. L. 108-357, § 802(b)(1), inserted “45,” before “46.”

2000—Subsec. (a). Pub. L. 106-519, § 4(2)(B), inserted at end “A rule similar to the rule of section 943(d) shall apply for purposes of paragraph (4)(C).”

Subsec. (a)(4)(C). Pub. L. 106-519, § 4(2)(A), added subpar. (C).

1987—Subsec. (a)(6). Pub. L. 100-203 substituted “46, and 54” for “and 46”.

1986—Subsec. (a). Pub. L. 99-499 inserted at end “Paragraph (1) shall not apply to the tax imposed by section 59A.”

1984—Subsec. (a)(4). Pub. L. 98-369, § 801(d)(5), inserted provision disallowing a deduction for income, war profits, and excess profits taxes if such taxes are paid or accrued with respect to foreign trade income, within the meaning of section 923(b), of a FSC.

Subsec. (a)(6). Pub. L. 98-369, § 67(b)(2), inserted reference to chapter 46.

1983—Subsec. (a). Pub. L. 98-21 inserted at end “Paragraph (1) shall not apply to any taxes to the extent such taxes are allowable as a deduction under section 164(f).”

Subsec. (a)(1). Pub. L. 98-67 repealed amendments made by Pub. L. 97-248. See 1982 Amendment note below.

1982—Subsec. (a)(1). Pub. L. 97-248 provided that, applicable to payments of interest, dividends, and patronage dividends paid or credited after June 30, 1983, par. (1) is amended by striking out “and” at end of subpar. (B), by substituting “; and” for the period at end of subpar. (C), and by inserting subpar. (D) relating to the tax withheld at source on interest, dividends, and pa-

tronage dividends under section 3451. Section 102(a), (b) of Pub. L. 98-67, title I, Aug. 5, 1983, 97 Stat. 369, repealed subtitle A (§§ 301-308) of title III of Pub. L. 97-248 as of the close of June 30, 1983, and provided that the Internal Revenue Code of 1954 [now 1986] [this title] shall be applied and administered (subject to certain exceptions) as if such subtitle A (and the amendments made by such subtitle A) had not been enacted.

1976—Subsec. (a)(1)(C). Pub. L. 94-455, § 1901(a)(39), struck out “, and corresponding provisions of prior revenue laws” after “under section 3402”.

Subsec. (a)(6). Pub. L. 94-455, §§ 1307(d)(2)(A), 1605(b)(1), inserted reference to chapters 41 and 44.

1974—Subsec. (a)(6). Pub. L. 93-406 added par. (6).

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by section 101(b)(5) of Pub. L. 108-357 applicable to transactions after Dec. 31, 2004, see section 101(c) of Pub. L. 108-357, set out as a note under section 56 of this title.

Amendment by section 802(b)(1) of Pub. L. 108-357 effective Mar. 4, 2003, see section 802(d) of Pub. L. 108-357, set out as an Effective Date note under section 4985 of this title.

EFFECTIVE DATE OF 2000 AMENDMENT

Amendment by Pub. L. 106-519 applicable to transactions after Sept. 30, 2000, with special rules relating to existing foreign sales corporations, see section 5 of Pub. L. 106-519, set out as a note under section 56 of this title.

EFFECTIVE DATE OF 1987 AMENDMENT

Amendment by Pub. L. 100-203 applicable to consideration received after Dec. 22, 1987, in taxable years ending after such date, except not applicable in the case of any acquisition pursuant to a written binding contract in effect on Dec. 15, 1987, and at all times thereafter before the acquisition, see section 10228(d) of Pub. L. 100-203, set out as an Effective Date note under section 5881 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99-499 applicable to taxable years beginning after Dec. 31, 1986, see section 516(c) of Pub. L. 99-499, set out as a note under section 26 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 67(b)(2) of Pub. L. 98-369 applicable to payments under agreements entered into or renewed after June 14, 1984, in taxable years ending after such date, with contracts entered into before June 15, 1984, which are amended after June 14, 1984, in any significant relevant aspect to be treated as a contract entered into after June 14, 1984, see section 67(e) of Pub. L. 98-369, set out as an Effective Date note under section 280G of this title.

Amendment by section 801(d)(5) of Pub. L. 98-369 applicable to transactions after Dec. 31, 1984, in taxable years ending after such date, see section 805(a)(1) of Pub. L. 98-369, as amended, set out as a note under section 245 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Amendment by Pub. L. 98-21 applicable to taxable years beginning after Dec. 31, 1989, see section 124(d)(2) of Pub. L. 98-21, set out as a note under section 1401 of this title.

EFFECTIVE DATE OF 1976 AMENDMENT

For effective date of amendment by section 1307(d)(2)(A) of Pub. L. 94-455, see section 1307(e) of Pub. L. 94-455, set out as a note under section 501 of this title.

For effective date of amendment by section 1605(b)(1) of Pub. L. 94-455, see section 1608(d) of Pub. L. 94-455, set out as a note under section 856 of this title.

Amendment by section 1901(a)(39) of Pub. L. 94-455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94-455, set out as a note under section 2 of this title.

EFFECTIVE DATE OF 1974 AMENDMENT

Amendment by Pub. L. 93-406 applicable, except as otherwise provided in section 1017(c) through (i) of Pub. L. 93-406, for plan years beginning after Sept. 2, 1974, but, in the case of plans in existence on Jan. 1, 1974, amendment by Pub. L. 93-406 applicable for plan years beginning after Dec. 31, 1975, see section 1017 of Pub. L. 93-406, set out as a note under section 410 of this title.

EFFECTIVE DATE

Section applicable to taxable years beginning after Dec. 31, 1963, see section 207(c) of Pub. L. 88-272, set out as an Effective Date of 1964 Amendment note under section 164 of this title.

§ 276. Certain indirect contributions to political parties

(a) Disallowance of deduction

No deduction otherwise allowable under this chapter shall be allowed for any amount paid or incurred for—

(1) advertising in a convention program of a political party, or in any other publication if any part of the proceeds of such publication directly or indirectly inures (or is intended to inure) to or for the use of a political party or a political candidate,

(2) admission to any dinner or program, if any part of the proceeds of such dinner or program directly or indirectly inures (or is intended to inure) to or for the use of a political party or a political candidate, or

(3) admission to an inaugural ball, inaugural gala, inaugural parade, or inaugural concert, or to any similar event which is identified with a political party or a political candidate.

(b) Definitions

For purposes of this section—

(1) Political party

The term “political party” means—

(A) a political party;

(B) a National, State, or local committee of a political party; or

(C) a committee, association, or organization, whether incorporated or not, which directly or indirectly accepts contributions (as defined in section 271(b)(2)) or make expenditures (as defined in section 271(b)(3)) for the purpose of influencing or attempting to influence the selection, nomination, or election of any individual to any Federal, State, or local elective public office, or the election of presidential and vice-presidential electors, whether or not such individual or electors are selected, nominated, or elected.

(2) Proceeds inuring to or for the use of political candidates

Proceeds shall be treated as inuring to or for the use of a political candidate only if—

(A) such proceeds may be used directly or indirectly for the purpose of furthering his candidacy for selection, nomination, or election to any elective public office, and

(B) such proceeds are not received by such candidate in the ordinary course of a trade

or business (other than the trade or business of holding elective public office).

(c) Cross reference

For disallowance of certain entertainment, etc., expenses, see section 274.

(Added Pub. L. 89-368, title III, §301(a), Mar. 15, 1966, 80 Stat. 66; amended Pub. L. 90-364, title I, §108(a), June 28, 1968, 82 Stat. 268; Pub. L. 93-443, title IV, §406(d), Oct. 15, 1974, 88 Stat. 1296.)

AMENDMENTS

1974—Subsecs. (c), (d). Pub. L. 93-443 struck out subsec. (c) relating to advertising in a convention program of a national political convention, and redesignated subsec. (d) as (c).

1968—Subsecs. (c), (d). Pub. L. 90-364 added subsec. (c) and redesignated former subsec. (c) as (d).

EFFECTIVE DATE OF 1974 AMENDMENT

Amendment by Pub. L. 93-443 applicable with respect to taxable years beginning after Dec. 31, 1974, see section 410(c)(1) of Pub. L. 93-443, set out as a note under section 431 of Title 2, The Congress.

EFFECTIVE DATE OF 1968 AMENDMENT

Section 108(b) of Pub. L. 90-364 provided that: “The amendments made by subsection (a) [amending this section] shall apply with respect to amounts paid or incurred on or after January 1, 1968.”

EFFECTIVE DATE

Section 301(c) of Pub. L. 89-368 provided that: “The amendments made by subsections (a) and (b) [enacting this section] shall apply to taxable years beginning after December 31, 1965, but only with respect to amounts paid or incurred after the date of the enactment of this Act [Mar. 15, 1966].”

PROGRAM ADVERTISING FOR PRESIDENTIAL AND VICE-PRESIDENTIAL NOMINATING CONVENTIONS

Pub. L. 90-346, June 18, 1968, 82 Stat. 183, provided for advertising in a convention program of a national political convention, applicable with respect to amounts paid or incurred on or after Jan. 1, 1968, prior to repeal by Pub. L. 93-625, §10(g), Jan. 3, 1975, 88 Stat. 2119.

§ 277. Deductions incurred by certain membership organizations in transactions with members

(a) General rule

In the case of a social club or other membership organization which is operated primarily to furnish services or goods to members and which is not exempt from taxation, deductions for the taxable year attributable to furnishing services, insurance, goods, or other items of value to members shall be allowed only to the extent of income derived during such year from members or transactions with members (including income derived during such year from institutes and trade shows which are primarily for the education of members). If for any taxable year such deductions exceed such income, the excess shall be treated as a deduction attributable to furnishing services, insurance, goods, or other items of value to members paid or incurred in the succeeding taxable year. The deductions provided by sections 243, 244, and 245 (relating to dividends received by corporations) shall not be allowed to any organization to which this section applies for the taxable year.

(b) Exceptions

Subsection (a) shall not apply to any organization—

(1) which for the taxable year is subject to taxation under subchapter H or L,

(2) which has made an election before October 9, 1969, under section 456(c) or which is affiliated with such an organization,

(3) which for each day of any taxable year is a national securities exchange subject to regulation under the Securities Exchange Act of 1934 or a contract market subject to regulation under the Commodity Exchange Act, or

(4) which is engaged primarily in the gathering and distribution of news to its members for publication.

(Added Pub. L. 91-172, title I, §121(b)(3)(A), Dec. 30, 1969, 83 Stat. 540; amended Pub. L. 94-568, §1(c), Oct. 20, 1976, 90 Stat. 2697; Pub. L. 99-514, title XVI, §1604(a), Oct. 22, 1986, 100 Stat. 2769.)

REFERENCES IN TEXT

The Securities Exchange Act of 1934, referred to in subsec. (b)(3), is act June 6, 1934, ch. 404, 48 Stat. 881, as amended, which is classified principally to chapter 2B (§78a et seq.) of Title 15, Commerce and Trade. For complete classification of this Act to the Code, see section 78a of Title 15 and Tables.

The Commodity Exchange Act, referred to in subsec. (b)(3), is act Sept. 21, 1922, ch. 369, 42 Stat. 998, as amended, which is classified generally to chapter 1 (§1 et seq.) of Title 7, Agriculture. For complete classification of this Act to the Code, see section 1 of Title 7 and Tables.

AMENDMENTS

1986—Subsec. (b)(4). Pub. L. 99-514 added par. (4).

1976—Subsec. (a). Pub. L. 94-568 provided that the deductions provided by sections 243, 244, and 245 (relating to dividends received by corporations) shall not be allowed to any organization to which this section applies for the taxable year.

EFFECTIVE DATE OF 1986 AMENDMENT

Section 1604(b) of Pub. L. 99-514 provided that: "The amendment made by this section [amending this section] shall apply to taxable years beginning after the date of the enactment of this Act [Oct. 22, 1986]."

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by Pub. L. 94-568 applicable to taxable years beginning after Oct. 20, 1976, see section 1(d) of Pub. L. 94-568, set out as a note under section 501 of this title.

EFFECTIVE DATE

Section applicable to taxable years beginning after Dec. 31, 1970, see section 121(g) of Pub. L. 91-172, set out as an Effective Date of 1969 Amendment note under section 511 of this title.

[§ 278. Repealed. Pub. L. 99-514, title VIII, § 803(b)(6), Oct. 22, 1986, 100 Stat. 2356]

Section, added Pub. L. 91-172, title II, §216(a), Dec. 30, 1969, 83 Stat. 573; amended Pub. L. 91-680, §1(a), (b), (d), Jan. 12, 1971, 84 Stat. 2064; Pub. L. 94-455, title II, §207(b)(1), (2), Oct. 4, 1976, 90 Stat. 1538, related to capital expenditures incurred in planting and developing citrus and almond groves, and certain capital expenditures of farming syndicates.

EFFECTIVE DATE OF REPEAL

If any interest costs incurred after Dec. 31, 1986, are attributable to costs incurred before Jan. 1, 1987, the repeal of this section is applicable to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954

and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of Pub. L. 99-514) or, if applicable, section 266 of such Code, see section 7831(d)(2) of Pub. L. 101-239, set out as an Effective Date note under section 263A of this title.

Repeal applicable to costs incurred after Dec. 31, 1986, in taxable years ending after such date, except as otherwise provided, see section 803(d) of Pub. L. 99-514, set out as an Effective Date note under section 263A of this title.

§ 279. Interest on indebtedness incurred by corporation to acquire stock or assets of another corporation

(a) General rule

No deduction shall be allowed for any interest paid or incurred by a corporation during the taxable year with respect to its corporate acquisition indebtedness to the extent that such interest exceeds—

(1) \$5,000,000, reduced by

(2) the amount of interest paid or incurred by such corporation during such year on obligations (A) issued after December 31, 1967, to provide consideration for an acquisition described in paragraph (1) of subsection (b), but (B) which are not corporate acquisition indebtedness.

(b) Corporate acquisition indebtedness

For purposes of this section, the term "corporate acquisition indebtedness" means any obligation evidenced by a bond, debenture, note, or certificate or other evidence of indebtedness issued after October 9, 1969, by a corporation (hereinafter in this section referred to as "issuing corporation") if—

(1) such obligation is issued to provide consideration for the acquisition of—

(A) stock in another corporation (hereinafter in this section referred to as "acquired corporation"), or

(B) assets of another corporation (hereinafter in this section referred to as "acquired corporation") pursuant to a plan under which at least two-thirds (in value) of all the assets (excluding money) used in trades and businesses carried on by such corporation are acquired,

(2) such obligation is either—

(A) subordinated to the claims of trade creditors of the issuing corporation generally, or

(B) expressly subordinated in right of payment to the payment of any substantial amount of unsecured indebtedness, whether outstanding or subsequently issued, of the issuing corporation,

(3) the bond or other evidence of indebtedness is either—

(A) convertible directly or indirectly into stock of the issuing corporation, or

(B) part of an investment unit or other arrangement which includes, in addition to such bond or other evidence of indebtedness, an option to acquire, directly or indirectly, stock in the issuing corporation, and

(4) as of a day determined under subsection (c)(1), either—

(A) the ratio of debt to equity (as defined in subsection (c)(2)) of the issuing corporation exceeds 2 to 1, or

(B) the projected earnings (as defined in subsection (c)(3)) do not exceed 3 times the annual interest to be paid or incurred (determined under subsection (c)(4)).

(c) Rules for application of subsection (b)(4)

For purposes of subsection (b)(4)—

(1) Time of determination

Determinations are to be made as of the last day of any taxable year of the issuing corporation in which it issues any obligation to provide consideration for an acquisition described in subsection (b)(1) of stock in, or assets of, the acquired corporation.

(2) Ratio of debt to equity

The term “ratio of debt to equity” means the ratio which the total indebtedness of the issuing corporation bears to the sum of its money and all its other assets (in an amount equal to their adjusted basis for determining gain) less such total indebtedness.

(3) Projected earnings

(A) The term “projected earnings” means the “average annual earnings” (as defined in subparagraph (B)) of—

- (i) the issuing corporation only, if clause (ii) does not apply, or
- (ii) both the issuing corporation and the acquired corporation, in any case where the issuing corporation has acquired control (as defined in section 368(c)), or has acquired substantially all of the properties, of the acquired corporation.

(B) The average annual earnings referred to in subparagraph (A) is, for any corporation, the amount of its earnings and profits for any 3-year period ending with the last day of a taxable year of the issuing corporation described in paragraph (1), computed without reduction for—

- (i) interest paid or incurred,
- (ii) depreciation or amortization allowed under this chapter,
- (iii) liability for tax under this chapter, and
- (iv) distributions to which section 301(c)(1) applies (other than such distributions from the acquired to the issuing corporation),

and reduced to an annual average for such 3-year period pursuant to regulations prescribed by the Secretary. Such regulations shall include rules for cases where any corporation was not in existence for all of such 3-year period or such period includes only a portion of a taxable year of any corporation.

(4) Annual interest to be paid or incurred

The term “annual interest to be paid or incurred” means—

- (A) if subparagraph (B) does not apply, the annual interest to be paid or incurred by the issuing corporation only, determined by reference to its total indebtedness outstanding, or
- (B) if projected earnings are determined under clause (ii) of paragraph (3)(A), the annual interest to be paid or incurred by both the issuing corporation and the acquired

corporation, determined by reference to their combined total indebtedness outstanding.

(5) Special rules for banks and lending or finance companies

With respect to any corporation which is a bank (as defined in section 581) or is primarily engaged in a lending or finance business—

(A) in determining under paragraph (2) the ratio of debt to equity of such corporation (or of the affiliated group of which such corporation is a member), the total indebtedness of such corporation (and the assets of such corporation) shall be reduced by an amount equal to the total indebtedness owed to such corporation which arises out of the banking business of such corporation, or out of the lending or finance business of such corporation, as the case may be;

(B) in determining under paragraph (4) the annual interest to be paid or incurred by such corporation (or by the issuing and acquired corporations referred to in paragraph (4)(B) or by the affiliated group of which such corporation is a member) the amount of such interest (determined without regard to this paragraph) shall be reduced by an amount which bears the same ratio to the amount of such interest as the amount of the reduction for the taxable year under subparagraph (A) bears to the total indebtedness of such corporation; and

(C) in determining under paragraph (3)(B) the average annual earnings, the amount of the earnings and profits for the 3-year period shall be reduced by the sum of the reductions under subparagraph (B) for such period.

For purposes of this paragraph, the term “lending or finance business” means a business of making loans or purchasing or discounting accounts receivable, notes, or installment obligations.

(d) Taxable years to which applicable

In applying this section—

(1) First year of disallowance

The deduction of interest on any obligation shall not be disallowed under subsection (a) before the first taxable year of the issuing corporation as of the last day of which the application of either subparagraph (A) or subparagraph (B) of subsection (b)(4) results in such obligation being corporate acquisition indebtedness.

(2) General rule for succeeding years

Except as provided in paragraphs (3), (4), and (5), if an obligation is determined to be corporate acquisition indebtedness as of the last day of any taxable year of the issuing corporation, it shall be corporate acquisition indebtedness for such taxable year and all subsequent taxable years.

(3) Redetermination where control, etc., is acquired

If an obligation is determined to be corporate acquisition indebtedness as of the close of a taxable year of the issuing corporation in

which clause (i) of subsection (c)(3)(A) applied, but would not be corporate acquisition indebtedness if the determination were made as of the close of the first taxable year of such corporation thereafter in which clause (ii) of subsection (c)(3)(A) could apply, such obligation shall be considered not to be corporate acquisition indebtedness for such later taxable year and all taxable years thereafter.

(4) Special 3-year rule

If an obligation which has been determined to be corporate acquisition indebtedness for any taxable year would not be such indebtedness for each of any 3 consecutive taxable years thereafter if subsection (b)(4) were applied as of the close of each of such 3 years, then such obligation shall not be corporate acquisition indebtedness for all taxable years after such 3 consecutive taxable years.

(5) 5 percent stock rule

In the case of obligations issued to provide consideration for the acquisition of stock in another corporation, such obligations shall be corporate acquisition indebtedness for a taxable year only if at some time after October 9, 1969, and before the close of such year the issuing corporation owns 5 percent or more of the total combined voting power of all classes of stock entitled to vote of such other corporation.

(e) Certain nontaxable transactions

An acquisition of stock of a corporation of which the issuing corporation is in control (as defined in section 368(c)) in a transaction in which gain or loss is not recognized shall be deemed an acquisition described in paragraph (1) of subsection (b) only if immediately before such transaction (1) the acquired corporation was in existence, and (2) the issuing corporation was not in control (as defined in section 368(c)) of such corporation.

(f) Exemption for certain acquisitions of foreign corporations

For purposes of this section, the term "corporate acquisition indebtedness" does not include any indebtedness issued to any person to provide consideration for the acquisition of stock in, or assets of, any foreign corporation substantially all of the income of which, for the 3-year period ending with the date of such acquisition or for such part of such period as the foreign corporation was in existence, is from sources without the United States.

(g) Affiliated groups

In any case in which the issuing corporation is a member of an affiliated group, the application of this section shall be determined, pursuant to regulations prescribed by the Secretary, by treating all of the members of the affiliated group in the aggregate as the issuing corporation, except that the ratio of debt to equity of, projected earnings of, and annual interest to be paid or incurred by any corporation (other than the issuing corporation determined without regard to this subsection) shall be included in the determinations required under subparagraphs (A) and (B) of subsection (b)(4) as of any day only if such corporation is a member of the af-

filiated group on such day, and, in determining projected earnings of such corporation under subsection (c)(3), there shall be taken into account only the earnings and profits of such corporation for the period during which it was a member of the affiliated group. For purposes of the preceding sentence, the term "affiliated group" has the meaning assigned to such term by section 1504(a), except that all corporations other than the acquired corporation shall be treated as includible corporations (without any exclusion under section 1504(b)) and the acquired corporation shall not be treated as an includible corporation.

(h) Changes in obligation

For purposes of this section—

(1) Any extension, renewal, or refinancing of an obligation evidencing a preexisting indebtedness shall not be deemed to be the issuance of a new obligation.

(2) Any obligation which is corporate acquisition indebtedness of the issuing corporation is also corporate acquisition indebtedness of any corporation which becomes liable for such obligation as guarantor, endorser, or indemnitor or which assumes liability for such obligation in any transaction.

(i) Certain obligations issued after October 9, 1969

For purposes of this section, an obligation shall not be corporate acquisition indebtedness if issued after October 9, 1969, to provide consideration for the acquisition of—

(1) stock or assets pursuant to a binding written contract which was in effect on October 9, 1969, and at all times thereafter before such acquisition, or

(2) stock in any corporation where the issuing corporation, on October 9, 1969, and at all times thereafter before such acquisition, owned at least 50 percent of the total combined voting power of all classes of stock entitled to vote of the acquired corporation.

(j) Effect on other provisions

No inference shall be drawn from any provision in this section that any instrument designated as a bond, debenture, note, or certificate or other evidence of indebtedness by its issuer represents an obligation or indebtedness of such issuer in applying any other provision of this title.

(Added Pub. L. 91-172, title IV, §411(a), Dec. 30, 1969, 83 Stat. 604; amended Pub. L. 94-455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834; Pub. L. 94-514, §1(a), Oct. 15, 1976, 90 Stat. 2443.)

AMENDMENTS

1976—Subsecs. (c)(3)(B), (g). Pub. L. 94-455 struck out "or his delegate" after "Secretary".

Subsec. (i). Pub. L. 94-514 struck out provisions that par. (2) would cease to apply when (at any time on or after October 9, 1969) the issuing corporation has acquired control (as defined in section 368(c)) of the acquired corporation.

EFFECTIVE DATE OF 1976 AMENDMENT

Section 1(b) of Pub. L. 94-514 provided that: "The amendment made by subsection (a) [amending this section] shall apply to taxable years ending after October 9, 1969. If refund or credit of any overpayment of in-

come tax resulting from the amendment made by subsection (a) [amending this section] is prevented on the date of the enactment of this Act [Oct. 15, 1976], or at any time within one year after such date, by the operation of any law or rule of law, refund or credit of such overpayment may, nevertheless, be made or allowed if claim therefor is filed within one year from such date.”

EFFECTIVE DATE

Section 411(c) of Pub. L. 91-172 provided that: “The amendments made by this section [enacting this section] shall apply to the determination of the allowability of the deduction of interest paid or incurred with respect to indebtedness incurred after October 9, 1969.”

[§ 280. Repealed. Pub. L. 99-514, title VIII, § 803(b)(2)(A), Oct. 22, 1986, 100 Stat. 2355]

Section, added Pub. L. 94-455, title II, § 210(a), Oct. 4, 1976, 90 Stat. 1544; amended Pub. L. 95-600, title VII, § 701(m)(2), Nov. 6, 1978, 92 Stat. 2907; Pub. L. 97-354, § 5(a)(25), Oct. 19, 1982, 96 Stat. 1694, related to certain expenditures incurred in the production of films, books, records, or similar property.

EFFECTIVE DATE OF REPEAL

If any interest costs incurred after Dec. 31, 1986, are attributable to costs incurred before Jan. 1, 1987, the repeal of this section is applicable to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954 and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of Pub. L. 99-514) or, if applicable, section 266 of such Code, see section 7831(d)(2) of Pub. L. 101-239, set out as an Effective Date note under section 263A of this title.

Repeal applicable to costs incurred after Dec. 31, 1986, in taxable years ending after such date, except as otherwise provided, see section 803(d) of Pub. L. 99-514, set out as an Effective Date note under section 263A of this title.

§ 280A. Disallowance of certain expenses in connection with business use of home, rental of vacation homes, etc.

(a) General rule

Except as otherwise provided in this section, in the case of a taxpayer who is an individual or an S corporation, no deduction otherwise allowable under this chapter shall be allowed with respect to the use of a dwelling unit which is used by the taxpayer during the taxable year as a residence.

(b) Exception for interest, taxes, casualty losses, etc.

Subsection (a) shall not apply to any deduction allowable to the taxpayer without regard to its connection with his trade or business (or with his income-producing activity).

(c) Exceptions for certain business or rental use; limitation on deductions for such use

(1) Certain business use

Subsection (a) shall not apply to any item to the extent such item is allocable to a portion of the dwelling unit which is exclusively used on a regular basis—

(A) as the principal place of business for any trade or business of the taxpayer,

(B) as a place of business which is used by patients, clients, or customers in meeting or

dealing with the taxpayer in the normal course of his trade or business, or

(C) in the case of a separate structure which is not attached to the dwelling unit, in connection with the taxpayer's trade or business.

In the case of an employee, the preceding sentence shall apply only if the exclusive use referred to in the preceding sentence is for the convenience of his employer. For purposes of subparagraph (A), the term “principal place of business” includes a place of business which is used by the taxpayer for the administrative or management activities of any trade or business of the taxpayer if there is no other fixed location of such trade or business where the taxpayer conducts substantial administrative or management activities of such trade or business.

(2) Certain storage use

Subsection (a) shall not apply to any item to the extent such item is allocable to space within the dwelling unit which is used on a regular basis as a storage unit for the inventory or product samples of the taxpayer held for use in the taxpayer's trade or business of selling products at retail or wholesale, but only if the dwelling unit is the sole fixed location of such trade or business.

(3) Rental use

Subsection (a) shall not apply to any item which is attributable to the rental of the dwelling unit or portion thereof (determined after the application of subsection (e)).

(4) Use in providing day care services

(A) In general

Subsection (a) shall not apply to any item to the extent that such item is allocable to the use of any portion of the dwelling unit on a regular basis in the taxpayer's trade or business of providing day care for children, for individuals who have attained age 65, or for individuals who are physically or mentally incapable of caring for themselves.

(B) Licensing, etc., requirement

Subparagraph (A) shall apply to items accruing for a period only if the owner or operator of the trade or business referred to in subparagraph (A)—

(i) has applied for (and such application has not been rejected),

(ii) has been granted (and such granting has not been revoked), or

(iii) is exempt from having,

a license, certification, registration, or approval as a day care center or as a family or group day care home under the provisions of any applicable State law. This subparagraph shall apply only to items accruing in periods beginning on or after the first day of the first month which begins more than 90 days after the date of the enactment of the Tax Reduction and Simplification Act of 1977.

(C) Allocation formula

If a portion of the taxpayer's dwelling unit used for the purposes described in subpara-

graph (A) is not used exclusively for those purposes, the amount of the expenses attributable to that portion shall not exceed an amount which bears the same ratio to the total amount of the items allocable to such portion as the number of hours the portion is used for such purposes bears to the number of hours the portion is available for use.

(5) Limitation on deductions

In the case of a use described in paragraph (1), (2), or (4), and in the case of a use described in paragraph (3) where the dwelling unit is used by the taxpayer during the taxable year as a residence, the deductions allowed under this chapter for the taxable year by reason of being attributed to such use shall not exceed the excess of—

- (A) the gross income derived from such use for the taxable year, over
- (B) the sum of—
 - (i) the deductions allocable to such use which are allowable under this chapter for the taxable year whether or not such unit (or portion thereof) was so used, and
 - (ii) the deductions allocable to the trade or business (or rental activity) in which such use occurs (but which are not allocable to such use) for such taxable year.

Any amount not allowable as a deduction under this chapter by reason of the preceding sentence shall be taken into account as a deduction (allocable to such use) under this chapter for the succeeding taxable year. Any amount taken into account for any taxable year under the preceding sentence shall be subject to the limitation of the 1st sentence of this paragraph whether or not the dwelling unit is used as a residence during such taxable year.

(6) Treatment of rental to employer

Paragraphs (1) and (3) shall not apply to any item which is attributable to the rental of the dwelling unit (or any portion thereof) by the taxpayer to his employer during any period in which the taxpayer uses the dwelling unit (or portion) in performing services as an employee of the employer.

(d) Use as residence

(1) In general

For purposes of this section, a taxpayer uses a dwelling unit during the taxable year as a residence if he uses such unit (or portion thereof) for personal purposes for a number of days which exceeds the greater of—

- (A) 14 days, or
- (B) 10 percent of the number of days during such year for which such unit is rented at a fair rental.

For purposes of subparagraph (B), a unit shall not be treated as rented at a fair rental for any day for which it is used for personal purposes.

(2) Personal use of unit

For purposes of this section, the taxpayer shall be deemed to have used a dwelling unit for personal purposes for a day if, for any part of such day, the unit is used—

(A) for personal purposes by the taxpayer or any other person who has an interest in such unit, or by any member of the family (as defined in section 267(c)(4) of the taxpayer or such other person;

(B) by any individual who uses the unit under an arrangement which enables the taxpayer to use some other dwelling unit (whether or not a rental is charged for the use of such other unit); or

(C) by any individual (other than an employee with respect to whose use section 119 applies), unless for such day the dwelling unit is rented for a rental which, under the facts and circumstances, is fair rental.

The Secretary shall prescribe regulations with respect to the circumstances under which use of the unit for repairs and annual maintenance will not constitute personal use under this paragraph, except that if the taxpayer is engaged in repair and maintenance on a substantially full time basis for any day, such authority shall not allow the Secretary to treat a dwelling unit as being used for personal use by the taxpayer on such day merely because other individuals who are on the premises on such day are not so engaged.

(3) Rental to family member, etc., for use as principal residence

(A) In general

A taxpayer shall not be treated as using a dwelling unit for personal purposes by reason of a rental arrangement for any period if for such period such dwelling unit is rented, at a fair rental, to any person for use as such person's principal residence.

(B) Special rules for rental to person having interest in unit

(i) Rental must be pursuant to shared equity financing agreement

Subparagraph (A) shall apply to a rental to a person who has an interest in the dwelling unit only if such rental is pursuant to a shared equity financing agreement.

(ii) Determination of fair rental

In the case of a rental pursuant to a shared equity financing agreement, fair rental shall be determined as of the time the agreement is entered into and by taking into account the occupant's qualified ownership interest.

(C) Shared equity financing agreement

For purposes of this paragraph, the term "shared equity financing agreement" means an agreement under which—

- (i) 2 or more persons acquire qualified ownership interests in a dwelling unit, and
- (ii) the person (or persons) holding 1 or more of such interests—

(I) is entitled to occupy the dwelling unit for use as a principal residence, and

(II) is required to pay rent to 1 or more other persons holding qualified ownership interests in the dwelling unit.

(D) Qualified ownership interest

For purposes of this paragraph, the term "qualified ownership interest" means an un-

divided interest for more than 50 years in the entire dwelling unit and appurtenant land being acquired in the transaction to which the shared equity financing agreement relates.

(4) Rental of principal residence

(A) In general

For purposes of applying subsection (c)(5) to deductions allocable to a qualified rental period, a taxpayer shall not be considered to have used a dwelling unit for personal purposes for any day during the taxable year which occurs before or after a qualified rental period described in subparagraph (B)(i), or before a qualified rental period described in subparagraph (B)(ii), if with respect to such day such unit constitutes the principal residence (within the meaning of section 121) of the taxpayer.

(B) Qualified rental period

For purposes of subparagraph (A), the term “qualified rental period” means a consecutive period of—

- (i) 12 or more months which begins or ends in such taxable year, or
- (ii) less than 12 months which begins in such taxable year and at the end of which such dwelling unit is sold or exchanged, and

for which such unit is rented, or is held for rental, at a fair rental.

(e) Expenses attributable to rental

(1) In general

In any case where a taxpayer who is an individual or an S corporation uses a dwelling unit for personal purposes on any day during the taxable year (whether or not he is treated under this section as using such unit as a residence), the amount deductible under this chapter with respect to expenses attributable to the rental of the unit (or portion thereof) for the taxable year shall not exceed an amount which bears the same relationship to such expenses as the number of days during each year that the unit (or portion thereof) is rented at a fair rental bears to the total number of days during such year that the unit (or portion thereof) is used.

(2) Exception for deductions otherwise allowable

This subsection shall not apply with respect to deductions which would be allowable under this chapter for the taxable year whether or not such unit (or portion thereof) was rented.

(f) Definitions and special rules

(1) Dwelling unit defined

For purposes of this section—

(A) In general

The term “dwelling unit” includes a house, apartment, condominium, mobile home, boat, or similar property, and all structures or other property appurtenant to such dwelling unit.

(B) Exception

The term “dwelling unit” does not include that portion of a unit which is used exclu-

sively as a hotel, motel, inn, or similar establishment.

(2) Personal use by shareholders of S corporation

In the case of an S corporation, subparagraphs (A) and (B) of subsection (d)(2) shall be applied by substituting “any shareholder of the S corporation” for “the taxpayer” each place it appears.

(3) Coordination with section 183

If subsection (a) applies with respect to any dwelling unit (or portion thereof) for the taxable year—

(A) section 183 (relating to activities not engaged in for profit) shall not apply to such unit (or portion thereof) for such year, but

(B) such year shall be taken into account as a taxable year for purposes of applying subsection (d) of section 183 (relating to 5-year presumption).

(4) Coordination with section 162(a)(2)

Nothing in this section shall be construed to disallow any deduction allowable under section 162(a)(2) (or any deduction which meets the tests of section 162(a)(2) but is allowable under another provision of this title) by reason of the taxpayer’s being away from home in the pursuit of a trade or business (other than the trade or business of renting dwelling units).

(g) Special rule for certain rental use

Notwithstanding any other provision of this section or section 183, if a dwelling unit is used during the taxable year by the taxpayer as a residence and such dwelling unit is actually rented for less than 15 days during the taxable year, then—

(1) no deduction otherwise allowable under this chapter because of the rental use of such dwelling unit shall be allowed, and

(2) the income derived from such use for the taxable year shall not be included in the gross income of such taxpayer under section 61.

(Added Pub. L. 94-455, title VI, §601(a), Oct. 4, 1976, 90 Stat. 1569; amended Pub. L. 95-30, title III, §306(a), (b), May 23, 1977, 91 Stat. 152, 153; Pub. L. 95-600, title VII, §701(h)(1), Nov. 6, 1978, 92 Stat. 2904; Pub. L. 97-119, title I, §113(a)-(d), Dec. 29, 1981, 95 Stat. 1641, 1642; Pub. L. 97-216, title II, §215(b), July 18, 1982, 96 Stat. 194; Pub. L. 97-354, §5(a)(26), Oct. 19, 1982, 96 Stat. 1694; Pub. L. 99-514, title I, §143(b), (c), Oct. 22, 1986, 100 Stat. 2120; Pub. L. 100-647, title I, §1001(h)(1), (2), Nov. 10, 1988, 102 Stat. 3352; Pub. L. 104-188, title I, §§1113(a), 1704(t)(39), Aug. 20, 1996, 110 Stat. 1759, 1889; Pub. L. 105-34, title III, §312(d)(1), title IX, §932(a), Aug. 5, 1997, 111 Stat. 839, 881.)

REFERENCES IN TEXT

The date of enactment of the Tax Reduction and Simplification Act of 1977, referred to in subsec. (c)(4)(B), is the date of enactment of Pub. L. 95-30, 91 Stat. 126, which was May 23, 1977.

AMENDMENTS

1997—Subsec. (c)(1). Pub. L. 105-34, §932(a), inserted at end “For purposes of subparagraph (A), the term ‘principal place of business’ includes a place of business which is used by the taxpayer for the administrative or

management activities of any trade or business of the taxpayer if there is no other fixed location of such trade or business where the taxpayer conducts substantial administrative or management activities of such trade or business.”

Subsec. (d)(4)(A). Pub. L. 105-34, §312(d)(1), substituted “section 121” for “section 1034”.

1996—Subsec. (c)(1)(A). Pub. L. 104-188, §1704(t)(39), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: “the principal place of business for any trade or business of the taxpayer.”

Subsec. (c)(2). Pub. L. 104-188, §1113(a), substituted “inventory or product samples” for “inventory”.

1988—Subsec. (c)(5). Pub. L. 100-647 inserted “(or rental activity)” after “trade or business” in subpar. (B)(ii) and inserted at end “Any amount taken into account for any taxable year under the preceding sentence shall be subject to the limitation of the 1st sentence of this paragraph whether or not the dwelling unit is used as a residence during such taxable year.”

1986—Subsec. (c)(5)(B). Pub. L. 99-514, §143(c), added subpar. (B) and struck out former subpar. (B) which read as follows: “the deductions allocable to such use which are allowable under this chapter for the taxable year whether or not such unit (or portion thereof) was so used.”

Subsec. (c)(6). Pub. L. 99-514, §143(b), added par. (6).
1982—Subsecs. (a), (e)(1). Pub. L. 97-354, §5(a)(26)(A), (B), substituted “an S corporation” for “an electing small business corporation”.

Subsec. (f)(2). Pub. L. 97-354, §5(a)(26)(C), substituted “shareholders of S corporation” for “electing small business corporation” in subsec. heading, substituted “an S corporation” for “an electing small business corporation” and “any shareholder of the S corporation” for “any shareholder of the electing small business corporation”.

Subsec. (f)(4). Pub. L. 97-216 struck out “, etc.” after “section 162(a)(2)” in heading, struck out “(A) In general.—” before “Nothing in this section”, and struck out subpar. (B) which directed the Secretary to prescribe amounts deductible (without substantiation) pursuant to last sentence of section 162(a) and that no other provisions of this title could permit such a deduction for any taxable year of amounts in excess of the amounts determined to be appropriate under the circumstances.

1981—Subsec. (c)(1)(A). Pub. L. 97-119, §113(c), substituted “the principal place of business for any trade or business of the taxpayer” for “as the taxpayer’s principal place of business”.

Subsec. (d)(2). Pub. L. 97-119, §113(d), inserted in provision following subpar. (C) “, except that if the taxpayer is engaged in repair and maintenance on a substantially full time basis for any day, such authority shall not allow the Secretary to treat a dwelling unit as being used for personal use by the taxpayer on such day merely because other individuals who are on the premises on such day are not so engaged”.

Subsec. (d)(3), (4). Pub. L. 97-119, §113(a), added par. (3), redesignated former par. (3) as (4) and struck out “to a person other than a member of the family (as defined in section 267(c)(4) of the taxpayer) after “such unit is rented” in subpar. (B).

Subsec. (f)(4). Pub. L. 97-119, §113(b)(1), added par. (4).
1978—Subsec. (d)(3). Pub. L. 95-600 added par. (3).

1977—Subsec. (c)(4), (5). Pub. L. 95-30 added par. (4), redesignated former par. (4) as (5) and substituted “paragraph (1), (2), or (4)” for “paragraph (1) or (2)” in introductory provisions.

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by section 312(d)(1) of Pub. L. 105-34 applicable to sales and exchanges after May 6, 1997, with certain exceptions, see section 312(d) of Pub. L. 105-34, set out as a note under section 121 of this title.

Section 932(b) of Pub. L. 105-34 provided that: “The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1998.”

EFFECTIVE DATE OF 1996 AMENDMENT

Section 1113(b) of Pub. L. 104-188 provided that: “The amendment made by subsection (a) [amending this section] shall apply to taxable years beginning after December 31, 1995.”

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99-514 applicable to taxable years beginning after Dec. 31, 1986, see section 151(a) of Pub. L. 99-514, set out as a note under section 1 of this title.

EFFECTIVE DATES OF 1982 AMENDMENTS

Amendment by Pub. L. 97-354 applicable to taxable years beginning after Dec. 31, 1982, see section 6(a) of Pub. L. 97-354, set out as an Effective Date note under section 1361 of this title.

Amendment by Pub. L. 97-216 applicable to taxable years beginning after Dec. 31, 1981, see section 215(d) of Pub. L. 97-216, set out as a note under section 162 of this title.

EFFECTIVE DATE OF 1981 AMENDMENT

Section 113(e) of Pub. L. 97-119 provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1975, except that in the case of taxable years beginning after December 31, 1975, and before January 1, 1980, the amendment made by this section shall apply only to taxable years for which, on the date of the enactment of this Act [Dec. 29, 1981], the making of a refund, or the assessment of a deficiency, was not barred by law or any rule of law.”

EFFECTIVE DATE OF 1978 AMENDMENT

Section 701(h)(2) of Pub. L. 95-600, as amended by Pub. L. 99-514, §2, Oct. 22, 1986, 100 Stat. 2095, provided that: “The amendment made by paragraph (1) [amending this section] shall take effect as if included in section 280A of the Internal Revenue Code of 1986 [formerly I.R.C. 1954], as such provision was added to such Code by section 601(a) of the Tax Reform Act of 1976 [Pub. L. 94-455, title VI, §601(a), Oct. 4, 1976, 90 Stat. 1569].”

EFFECTIVE DATE OF 1977 AMENDMENT

Section 306(c) of Pub. L. 95-30 provided that: “The amendments made by this section [amending this section] shall apply to taxable years beginning after December 31, 1975.”

EFFECTIVE DATE

Section 601(c) of Pub. L. 94-455 provided that: “The amendments made by this section [enacting this section and amending the analysis of sections preceding section 261 of this title] shall apply to taxable years beginning after December 31, 1975.”

§ 280B. Demolition of structures

In the case of the demolition of any structure—

(1) no deduction otherwise allowable under this chapter shall be allowed to the owner or lessee of such structure for—

(A) any amount expended for such demolition, or

(B) any loss sustained on account of such demolition; and

(2) amounts described in paragraph (1) shall be treated as properly chargeable to capital

account with respect to the land on which the demolished structure was located.

(Added Pub. L. 94-455, title XXI, §2124(b)(1), Oct. 4, 1976, 90 Stat. 1918; amended Pub. L. 95-600, title VII, §701(f)(5), Nov. 6, 1978, 92 Stat. 2902; Pub. L. 96-541, §2(b), Dec. 17, 1980, 94 Stat. 3204; Pub. L. 97-34, title II, §212(d)(2)(C), Aug. 13, 1981, 95 Stat. 239; Pub. L. 98-369, div. A, title X, §1063(a), (b)(1), July 18, 1984, 98 Stat. 1047.)

AMENDMENTS

1984—Pub. L. 98-369 struck out “certain historic” before “structures” in section catchline, struck out heading “(a) General rule”, substituted “In the case of the demolition of any structure” for “In the case of the demolition of a certified historic structure (as defined in 48(g)(3)(A))” in text, and struck out subssecs. (b) and (c) which contained provisions relating to a special rule for registered historic districts and to the application of this section, respectively.

1981—Subsec. (a). Pub. L. 97-34, §212(d)(2)(C)(i), substituted “48(g)(3)(A)” for “section 191(d)(1)” in provisions preceding par. (1).

Subsec. (b). Pub. L. 97-34, §212(d)(2)(C)(ii), substituted “section 48(g)(3)(B)” for “section 191(d)(2)”.

1980—Subsec. (c). Pub. L. 96-541 added subsec. (c).

1978—Subsec. (b). Pub. L. 95-600 substituted “registered historic district (as defined in section 191(d)(2))” for “Registered Historic District” and “Secretary of the Interior has certified that such structure is not a certified historic structure, and that such structure is not of historic significance to the district, and if such certification occurs after the beginning of the demolition of such structure, the taxpayer has certified to the Secretary that, at the time of such demolition, he in good faith was not aware of the certification requirement by the Secretary of the Interior” for “Secretary of the Interior has certified, prior to the demolition of such structure, that such structure is not of historic significance to the district”.

EFFECTIVE DATE OF 1984 AMENDMENT

Section 1063(c) of Pub. L. 98-369, as amended by Pub. L. 99-514, title XVIII, §1878(h), Oct. 22, 1986, 100 Stat. 2904, provided that:

“(1) The amendments made by this section [amending this section] shall apply to taxable years ending after December 31, 1983, but shall not apply to any demolition (other than of a certified historic structure) commencing before July 19, 1984.

“(2) For purposes of paragraph (1), if a demolition is delayed until the completion of the replacement structure on the same site, the demolition shall be treated as commencing when construction of the replacement structure commences.

“(3) The amendments made by this section [amending this section] shall not apply to any demolition commencing before September 1, 1984, pursuant to a bank headquarters building project if—

“(A) on April 1, 1984, a corporation was retained to advise the bank on the final completion of the project, and

“(B) on June 12, 1984, the Comptroller of the Currency approved the project.

“(4) The amendments made by this section shall not apply to the remaining adjusted basis at the time of demolition of any structure if—

“(A) such structure was used in the manufacture, storage, or distribution of lead alkyl antiknock products and intermediate and related products at facilities located in or near Baton Rouge, Louisiana, and Houston, Texas, owned by the same corporation, and

“(B) demolition of at least one such structure at the Baton Rouge facility commenced before January 1, 1984.”

EFFECTIVE DATE OF 1981 AMENDMENT

Amendment by Pub. L. 97-34 applicable to expenditures incurred after Dec. 31, 1981, in taxable years end-

ing after such date, see section 212(e) of Pub. L. 97-34, set out as a note under section 46 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Amendment by Pub. L. 95-600 effective as if included within the enactment of this section by section 2124 of Pub. L. 94-455, see section 701(f)(8) of Pub. L. 95-600, set out as an Effective and Termination Dates of 1978 Amendments note under section 167 of this title.

EFFECTIVE DATE

Section 2124(b)(3) of Pub. L. 94-455, which had provided that enactment of this section by subsec. (b) shall apply with respect to demolitions commencing after June 30, 1976, and before Jan. 1, 1981, was repealed by Pub. L. 96-541, §2(e)(2), Dec. 17, 1980, 94 Stat. 3205. See subsec. (c) of this section.

§ 280C. Certain expenses for which credits are allowable

(a) Rule for employment credits

No deduction shall be allowed for that portion of the wages or salaries paid or incurred for the taxable year which is equal to the sum of the credits determined for the taxable year under sections 45A(a), 45P(a), 51(a), and¹ 1396(a), 1400P(b), and 1400R. In the case of a corporation which is a member of a controlled group of corporations (within the meaning of section 52(a)) or a trade or business which is treated as being under common control with other trades or businesses (within the meaning of section 52(b)), this subsection shall be applied under rules prescribed by the Secretary similar to the rules applicable under subsections (a) and (b) of section 52.

(b) Credit for qualified clinical testing expenses for certain drugs

(1) In general

No deduction shall be allowed for that portion of the qualified clinical testing expenses (as defined in section 45C(b)) otherwise allowable as a deduction for the taxable year which is equal to the amount of the credit allowable for the taxable year under section 45C (determined without regard to section 38(c)).

(2) Similar rule where taxpayer capitalizes rather than deducts expenses

If—

(A) the amount of the credit allowable for the taxable year under section 45C (determined without regard to section 38(c)), exceeds

(B) the amount allowable as a deduction for the taxable year for qualified clinical testing expenses (determined without regard to paragraph (1)),

the amount chargeable to capital account for the taxable year for such expenses shall be reduced by the amount of such excess.

(3) Controlled groups

In the case of a corporation which is a member of a controlled group of corporations (within the meaning of section 41(f)(5)) or a trade or business which is treated as being under common control with other trades or business (within the meaning of section

¹ So in original. The word “and” probably should not appear.

41(f)(1)(B)), this subsection shall be applied under rules prescribed by the Secretary similar to the rules applicable under subparagraphs (A) and (B) of section 41(f)(1).

(c) Credit for increasing research activities

(1) In general

No deduction shall be allowed for that portion of the qualified research expenses (as defined in section 41(b)) or basic research expenses (as defined in section 41(e)(2)) otherwise allowable as a deduction for the taxable year which is equal to the amount of the credit determined for such taxable year under section 41(a).

(2) Similar rule where taxpayer capitalizes rather than deducts expenses

If—

(A) the amount of the credit determined for the taxable year under section 41(a)(1), exceeds

(B) the amount allowable as a deduction for such taxable year for qualified research expenses or basic research expenses (determined without regard to paragraph (1)),

the amount chargeable to capital account for the taxable year for such expenses shall be reduced by the amount of such excess.

(3) Election of reduced credit

(A) In general

In the case of any taxable year for which an election is made under this paragraph—

(i) paragraphs (1) and (2) shall not apply, and

(ii) the amount of the credit under section 41(a) shall be the amount determined under subparagraph (B).

(B) Amount of reduced credit

The amount of credit determined under this subparagraph for any taxable year shall be the amount equal to the excess of—

(i) the amount of credit determined under section 41(a) without regard to this paragraph, over

(ii) the product of—

(I) the amount described in clause (i), and

(II) the maximum rate of tax under section 11(b)(1).

(C) Election

An election under this paragraph for any taxable year shall be made not later than the time for filing the return of tax for such year (including extensions), shall be made on such return, and shall be made in such manner as the Secretary may prescribe. Such an election, once made, shall be irrevocable.

(4) Controlled groups

Paragraph (3) of subsection (b) shall apply for purposes of this subsection.

(d) Credit for low sulfur diesel fuel production

The deductions otherwise allowed under this chapter for the taxable year shall be reduced by the amount of the credit determined for the taxable year under section 45H(a).

(e) Mine rescue team training credit

No deduction shall be allowed for that portion of the expenses otherwise allowable as a deduc-

tion for the taxable year which is equal to the amount of the credit determined for the taxable year under section 45N(a).

(f) Credit for security of agricultural chemicals

No deduction shall be allowed for that portion of the expenses otherwise allowable as a deduction taken into account in determining the credit under section 45O for the taxable year which is equal to the amount of the credit determined for such taxable year under section 45O(a).

(Added Pub. L. 95-30, title II, §202(c)(1), May 23, 1977, 91 Stat. 147; amended Pub. L. 95-600, title III, §322(d)(1), Nov. 6, 1978, 92 Stat. 2838; Pub. L. 96-178, §6(c)(4), Jan. 2, 1980, 93 Stat. 1298; Pub. L. 96-222, title I, §103(a)(7)(D)(iv), Apr. 1, 1980, 94 Stat. 212; Pub. L. 97-414, §4(b)(1), (2)(A), Jan. 4, 1983, 96 Stat. 2055; Pub. L. 98-369, div. A, title IV, §474(r)(10), July 18, 1984, 98 Stat. 841; Pub. L. 99-514, title II, §231(d)(3)(E), title XVIII, §1847(b)(8), Oct. 22, 1986, 100 Stat. 2179, 2856; Pub. L. 100-647, title IV, §4008(a), Nov. 10, 1988, 102 Stat. 3652; Pub. L. 101-239, title VII, §§7110(c)(1), 7814(e)(2)(A), Dec. 19, 1989, 103 Stat. 2325, 2413; Pub. L. 103-66, title XIII, §§13302(b)(1), 13322(c)(1), Aug. 10, 1993, 107 Stat. 555, 563; Pub. L. 104-188, title I, §1205(d)(7), Aug. 20, 1996, 110 Stat. 1776; Pub. L. 106-170, title V, §502(c)(2), Dec. 17, 1999, 113 Stat. 1919; Pub. L. 106-554, §1(a)(7) [title III, §311(a)(1)], Dec. 21, 2000, 114 Stat. 2763, 2763A-639; Pub. L. 108-357, title III, §339(c), Oct. 22, 2004, 118 Stat. 1484; Pub. L. 109-135, title I, §103(b)(2), title II, §201(b)(2), Dec. 21, 2005, 119 Stat. 2595, 2607; Pub. L. 109-432, div. A, title IV, §405(c), Dec. 20, 2006, 120 Stat. 2957; Pub. L. 110-172, §7(a)(1)(B), Dec. 29, 2007, 121 Stat. 2481; Pub. L. 110-234, title XV, §15343(c), May 22, 2008, 122 Stat. 1519; Pub. L. 110-245, title I, §111(c), June 17, 2008, 122 Stat. 1635; Pub. L. 110-246, §4(a), title XV, §15343(c), June 18, 2008, 122 Stat. 1664, 2281.)

CODIFICATION

Pub. L. 110-234 and Pub. L. 110-246 made identical amendments to this section. The amendments by Pub. L. 110-234 were repealed by section 4(a) of Pub. L. 110-246.

AMENDMENTS

2008—Subsec. (a). Pub. L. 110-245 inserted “45P(a),” after “45A(a),”.

Subsec. (f). Pub. L. 110-246, §15343(c), added subsec. (f).

2007—Subsec. (d). Pub. L. 110-172 amended heading and text generally. Prior to amendment, text read as follows: “No deduction shall be allowed for that portion of the expenses otherwise allowable as a deduction for the taxable year which is equal to the amount of the credit determined for the taxable year under section 45H(a).”

2006—Subsec. (e). Pub. L. 109-432 added subsec. (e).

2005—Subsec. (a). Pub. L. 109-135, §201(b)(2), substituted “1400P(b), and 1400R” for “and 1400P(b)”.

Pub. L. 109-135, §103(b)(2), substituted “1396(a), and 1400P(b)” for “and 1396(a)”.

2004—Subsec. (d). Pub. L. 108-357 added subsec. (d).

2000—Subsec. (c)(1). Pub. L. 106-554 struck out “or credit” after “deduction” in two places.

1999—Subsec. (c)(1). Pub. L. 106-170 inserted “or credit” after “deduction” in two places.

1996—Subsec. (b)(1). Pub. L. 104-188, §1205(d)(7), substituted “section 45C(b)” for “section 28(b)”, “section 45C” for “section 28”, and “section 38(c)” for “subsection (d)(2) thereof”.

Subsec. (b)(2)(A). Pub. L. 104-188, §1205(d)(7)(B), (C), substituted “section 45C” for “section 28” and “section 38(c)” for “subsection (d)(2) thereof”.

1993—Subsec. (a). Pub. L. 103-66, §13322(c)(1), substituted “45A(a), 51(a), and” for “51(a)”.

Pub. L. 103-66, §13302(b)(1), substituted “Rule for employment credits” for “Rule for targeted jobs credit” in heading and “the sum of the credits determined for the taxable year under sections 51(a) and 1396(a)” for “the amount of the credit determined for the taxable year under section 51(a)” in text.

1989—Subsec. (c)(1), (2)(A). Pub. L. 101-239, §7110(c)(1), struck out “50 percent of” before “the amount of the credit”.

Subsec. (c)(3). Pub. L. 101-239, §7814(e)(2)(A), added par. (3). Former par. (3) redesignated (4).

Subsec. (c)(3)(B)(ii)(I). Pub. L. 101-239, §7110(c)(1), struck out “50 percent of” before “the amount described”.

Subsec. (c)(4). Pub. L. 101-239, §7814(e)(2)(A), redesignated par. (3) as (4).

1988—Subsec. (c). Pub. L. 100-647 added subsec. (c).

1986—Subsec. (b)(1), (2)(A). Pub. L. 99-514, §1847(b)(8), substituted “section 28(b)” for “section 29(b)” in par. (1) and “section 28” for “section 29” in pars. (1) and (2)(A).

Subsec. (b)(3). Pub. L. 99-514, §231(d)(3)(E), substituted “section 41(f)(5)”, “section 41(f)(1)(B)”, and “section 41(f)(1)” for “section 30(f)(5)”, “section 30(f)(1)(B)”, and “section 30(f)(1)”, respectively.

1984—Subsec. (a). Pub. L. 98-369, §474(r)(10)(A), (B), redesignated subsec. (b) as (a), in heading substituted “targeted jobs credit” for “section 44B credit”, and in text substituted “No deduction shall be allowed for that portion of the wages or salaries paid or incurred for the taxable year which is equal to the amount of the credit determined for the taxable year under section 51(a)” for “No deduction shall be allowed for that portion of the wage or salaries paid or incurred for the taxable year which is equal to the amount of the credit allowable for the taxable year under section 44B (relating to credit for employment of certain new employees) determined without regard to the provisions of section 53 (relating to limitation based on amount of tax)”. Former subsec. (a), which had provided that no deduction would be allowed for that portion of the work incentive program expenses paid or incurred for the taxable year which was equal to the amount of the credit allowable for the taxable year under section 40 (relating to credit for expenses of work incentive programs) determined without regard to the provisions of section 50A(a)(2) (relating to limitation based on amount of tax), and that in the case of a corporation which was a member of a controlled group of corporations (within the meaning of section 50B(g)(1) or a trade or business which was treated as being under common control with other trades or businesses within the meaning of section 50B(g)(2), this subsection would be applied under rules prescribed by the Secretary similar to the rules applicable under paragraphs (1) and (2) of section 50B(g), was struck out.

Subsec. (b). Pub. L. 98-369, §474(r)(10)(A), redesignated subsec. (c) as (b). Former subsec. (b) redesignated (a).

Subsec. (b)(1), (2)(A). Pub. L. 98-369, §474(r)(10)(C), substituted “29” for “44H”.

Subsec. (b)(3). Pub. L. 98-369, §474(r)(10)(D), substituted “section 30(f)(5)” for “section 44F(f)(5)”, “section 30(f)(1)(B)” for “section 44F(f)(1)(B)”, and “section 30(f)(1)” for “section 44F(f)(1)”.

Subsec. (c). Pub. L. 98-369, §474(r)(10)(A), redesignated subsec. (c) as (b).

1983—Pub. L. 97-414, §4(b)(2)(A), substituted “Certain expenses for which credits are allowable” for “Portion of wages for which credit is claimed under section 40 or 44B” in section catchline.

Subsec. (c). Pub. L. 97-414, §4(b)(1), added subsec. (c). 1978—Pub. L. 95-600, as amended by Pub. L. 96-178 and Pub. L. 96-222, substituted “section 40 or 44B” for “section 44B” in section catchline, and in text designated existing provisions as subsec. (b) and added subsec. (a).

EFFECTIVE DATE OF 2008 AMENDMENT

Amendment of this section and repeal of Pub. L. 110-234 by Pub. L. 110-246 effective May 22, 2008, the

date of enactment of Pub. L. 110-234, except as otherwise provided, see section 4 of Pub. L. 110-246, set out as an Effective Date note under section 8701 of Title 7, Agriculture.

Amendment by section 15343(c) of Pub. L. 110-246 applicable to amounts paid or incurred after June 18, 2008, see section 15343(e) of Pub. L. 110-246, set out as a note under section 38 of this title.

Amendment by Pub. L. 110-245 applicable to amounts paid after June 17, 2008, see section 111(e) of Pub. L. 110-245, set out as a note under section 38 of this title.

EFFECTIVE DATE OF 2007 AMENDMENT

Amendment by Pub. L. 110-172 effective as if included in the provision of the American Jobs Creation Act of 2004, Pub. L. 108-357, to which such amendment relates, see section 7(e) of Pub. L. 110-172, set out as a note under section 1092 of this title.

EFFECTIVE DATE OF 2006 AMENDMENT

Amendment by Pub. L. 109-432 applicable to taxable years beginning after Dec. 31, 2005, see section 405(e) of Pub. L. 109-432, set out as a note under section 38 of this title.

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108-357 applicable to expenses paid or incurred after Dec. 31, 2002, in taxable years ending after such date, see section 339(f) of Pub. L. 108-357, set out as a note under section 38 of this title.

EFFECTIVE DATE OF 2000 AMENDMENT

Amendment by Pub. L. 106-554 effective as if included in the provisions of the Ticket to Work and Work Incentives Improvement Act of 1999, Pub. L. 106-170, to which such amendment relates, see section 1(a)(7) [title III, §311(d)] of Pub. L. 106-554, set out as a note under section 30A of this title.

EFFECTIVE DATE OF 1999 AMENDMENT

Amendment by Pub. L. 106-170 applicable to amounts paid or incurred after June 30, 1999, see section 502(c)(3) of Pub. L. 106-170, set out as a note under section 41 of this title.

EFFECTIVE DATE OF 1996 AMENDMENT

Amendment by Pub. L. 104-188 applicable to amounts paid or incurred in taxable years ending after June 30, 1996, see section 1205(e) of Pub. L. 104-188, set out as a note under section 45K of this title.

EFFECTIVE DATE OF 1993 AMENDMENT

Amendment by section 13322(c)(1) of Pub. L. 103-66 applicable to wages paid or incurred after Dec. 31, 1993, see section 13322(f) of Pub. L. 103-66, set out as a note under section 38 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by section 7110(c)(1) of Pub. L. 101-239 applicable to taxable years beginning after Dec. 31, 1989, see section 7110(e) of Pub. L. 101-239, set out as a note under section 41 of this title.

Amendment by section 7814(e)(2)(A) of Pub. L. 101-239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100-647, to which such amendment relates, see section 7817 of Pub. L. 101-239, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 applicable to taxable years beginning after Dec. 31, 1988, see section 4008(d) of Pub. L. 100-647, set out as a note under section 41 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 231(d)(3)(E) of Pub. L. 99-514 applicable to taxable years beginning after Dec. 31,

1985, see section 231(g) of Pub. L. 99-514, set out as a note under section 41 of this title.

Amendment by section 1847(b)(8) of Pub. L. 99-514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98-369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99-514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by Pub. L. 98-369 applicable to taxable years beginning after Dec. 31, 1983, and to carrybacks from such years, see section 475(a) of Pub. L. 98-369, set out as a note under section 21 of this title.

EFFECTIVE DATE OF 1983 AMENDMENT

Amendment by Pub. L. 97-414 applicable to amounts paid or incurred after December 31, 1982, in taxable years ending after such date, see section 4(d) of Pub. L. 97-414, set out as an Effective Date note under section 28 of this title.

EFFECTIVE DATE OF 1978 AMENDMENT

Section 322(e) of Pub. L. 95-600, as amended by Pub. L. 96-178, § 6(a), (b), Jan. 2, 1980, 93 Stat. 1297; Pub. L. 96-222, title I, § 103(a)(7)(A), (B), Apr. 1, 1980, 94 Stat. 211; Pub. L. 99-514, § 2, Oct. 22, 1986, 100 Stat. 2095, provided that:

“(1) IN GENERAL.—Except as otherwise provided in this subsection, the amendments made by this section [amending this section and sections 50A and 50B of this title] shall apply to work incentive program expenses paid or incurred after December 31, 1978, in taxable years ending after such date; except that so much of the amendment made by subsection (a) as affects section 50A(a)(2) of the Internal Revenue Code of 1986 [formerly I.R.C. 1954] shall apply to taxable years beginning after December 31, 1978. For purposes of applying section 50A(a)(2) of the Internal Revenue Code of 1986 with respect to a taxable year beginning before January 1, 1979, the rules of sections 50A(a)(4), 50A(a)(5), and 50B(e)(3) of such Code (as in effect on the day before the date of the enactment of this Act [Nov. 6, 1978] shall apply.

“(2) SPECIAL RULES FOR CERTAIN ELIGIBLE EMPLOYEES.—

“(A) ELIGIBLE EMPLOYEES HIRED BEFORE SEPTEMBER 27, 1978.—In the case of any eligible employee (as defined in section 50B(h)) hired before September 27, 1978, no credit shall be allowed under section 40 with respect to second-year work incentive program expenses (as defined in section 50B(a)) attributable to service performed by such employee.

“(B) ELIGIBLE EMPLOYEES HIRED AFTER SEPTEMBER 26, 1978.—In the case of any eligible employee (as defined in section 50B(h)) hired after September 26, 1978, for purposes of applying the amendments made by this section, such individual shall be treated for purposes of the credit allowed by section 40 as having first begun work for the taxpayer not earlier than January 1, 1979, and any wages paid or incurred after December 31, 1978, with respect to such individual shall be considered to be attributable to services rendered after that date.”

[Section 6(d) of Pub. L. 96-178 provided that: “Any amendment made by this section to the Revenue Act of 1978 [amending section 322(e)(1) and (2) of Pub. L. 95-600, set out above] shall take effect as if it had been included in the provision of the Revenue Act of 1978 [Pub. L. 95-600] to which such amendment relates.”]

EFFECTIVE DATE

Section applicable to taxable years beginning after Dec. 31, 1976, and to credit carrybacks from such years, see section 202(e) of Pub. L. 95-30, set out as a note under section 51 of this title.

TIME AND FORM OF CERTAIN ELECTIONS UNDER SUBSECTION (c)(3)

Section 7814(e)(2)(B) of Pub. L. 101-239 provided that: “In the case of a taxable year for which the last date

for making the election under section 280C(c)(3) of the Internal Revenue Code of 1986 (as added by subparagraph (A)) is on or before the date which is 75 days after the date of the enactment of this Act [Dec. 19, 1989], such an election for such year may be made—

“(i) at any time before the date which is 75 days after such date of enactment, and

“(ii) in such form and manner as the Secretary of the Treasury or his delegate may prescribe.”

PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§1101-1147 and 1171-1177] or title XVIII [§§1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

§ 280D. Repealed. Pub. L. 100-418, title I, § 1941(b)(4)(A), Aug. 23, 1988, 102 Stat. 1324]

Section, added Pub. L. 96-499, title XI, § 1131(d)(1), Dec. 5, 1980, 94 Stat. 2693, related to portion of chapter 45 windfall profit tax on domestic crude oil for which credit or refund was allowable under section 6429.

EFFECTIVE DATE OF REPEAL

Repeal applicable to crude oil removed from the premises on or after Aug. 23, 1988, see section 1941(c) of Pub. L. 100-418, set out as an Effective Date of 1988 Amendment note under section 164 of this title.

§ 280E. Expenditures in connection with the illegal sale of drugs

No deduction or credit shall be allowed for any amount paid or incurred during the taxable year in carrying on any trade or business if such trade or business (or the activities which comprise such trade or business) consists of trafficking in controlled substances (within the meaning of schedule I and II of the Controlled Substances Act) which is prohibited by Federal law or the law of any State in which such trade or business is conducted.

(Added Pub. L. 97-248, title III, § 351(a), Sept. 3, 1982, 96 Stat. 640.)

REFERENCES IN TEXT

The Controlled Substances Act, referred to in text, is title II of Pub. L. 91-513, Oct. 27, 1970, 84 Stat. 1242, as amended, which is classified principally to subchapter I (§ 801 et seq.) of chapter 13 of Title 21, Food and Drugs. Schedules I and II are set out in section 812 of Title 21. For complete classification of this Act to the Code, see Short Title note set out under section 801 of Title 21 and Tables.

EFFECTIVE DATE

Section 351(c) of Pub. L. 97-248 provided that: “The amendments made by this section [enacting this section] shall apply to amounts paid or incurred after the date of the enactment of this Act [Sept. 3, 1982] in taxable years ending after such date.”

§ 280F. Limitation on depreciation for luxury automobiles; limitation where certain property used for personal purposes

(a) Limitation on amount of depreciation for luxury automobiles

(1) Depreciation

(A) Limitation

The amount of the depreciation deduction for any taxable year for any passenger automobile shall not exceed—

- (i) \$2,560 for the 1st taxable year in the recovery period,
- (ii) \$4,100 for the 2nd taxable year in the recovery period,
- (iii) \$2,450 for the 3rd taxable year in the recovery period, and
- (iv) \$1,475 for each succeeding taxable year in the recovery period.

(B) Disallowed deductions allowed for years after recovery period

(i) In general

Except as provided in clause (ii), the unrecovered basis of any passenger automobile shall be treated as an expense for the 1st taxable year after the recovery period. Any excess of the unrecovered basis over the limitation of clause (ii) shall be treated as an expense in the succeeding taxable year.

(ii) \$1,475 limitation

The amount treated as an expense under clause (i) for any taxable year shall not exceed \$1,475.

(iii) Property must be depreciable

No amount shall be allowable as a deduction by reason of this subparagraph with respect to any property for any taxable year unless a depreciation deduction would be allowable with respect to such property for such taxable year.

(iv) Amount treated as depreciation deduction

For purposes of this subtitle, any amount allowable as a deduction by reason of this subparagraph shall be treated as a depreciation deduction allowable under section 168.

(C) Special rule for certain clean-fuel passenger automobiles

(i) Modified automobiles

In the case of a passenger automobile which is propelled by a fuel which is not a clean-burning fuel and to which is installed qualified clean-fuel vehicle property (as defined in section 179A(c)(1)(A)) for purposes of permitting such vehicle to be propelled by a clean burning fuel (as defined in section 179A(e)(1)), subparagraph (A) shall not apply to the cost of the installed qualified clean burning vehicle property.

(ii) Purpose built passenger vehicles

In the case of a purpose built passenger vehicle (as defined in section 4001(a)(2)(C)(ii)), each of the annual limitations specified in subparagraphs (A) and (B) shall be tripled.

(iii) Application of subparagraph

This subparagraph shall apply to property placed in service after August 5, 1997, and before January 1, 2007.

(2) Coordination with reductions in amount allowable by reason of personal use, etc.

This subsection shall be applied before—

- (A) the application of subsection (b), and

(B) the application of any other reduction in the amount of any depreciation deduction allowable under section 168 by reason of any use not qualifying the property for such credit or depreciation deduction.

(b) Limitation where business use of listed property not greater than 50 percent

(1) Depreciation

If any listed property is not predominantly used in a qualified business use for any taxable year, the deduction allowed under section 168 with respect to such property for such taxable year and any subsequent taxable year shall be determined under section 168(g) (relating to alternative depreciation system).

(2) Recapture

(A) Where business use percentage does not exceed 50 percent

If—

- (i) property is predominantly used in a qualified business use in a taxable year in which it is placed in service, and
- (ii) such property is not predominantly used in a qualified business use for any subsequent taxable year,

then any excess depreciation shall be included in gross income for the taxable year referred to in clause (ii), and the depreciation deduction for the taxable year referred to in clause (ii) and any subsequent taxable years shall be determined under section 168(g) (relating to alternative depreciation system).

(B) Excess depreciation

For purposes of subparagraph (A), the term “excess depreciation” means the excess (if any) of—

- (i) the amount of the depreciation deductions allowable with respect to the property for taxable years before the 1st taxable year in which the property was not predominantly used in a qualified business use, over
- (ii) the amount which would have been so allowable if the property had not been predominantly used in a qualified business use for the taxable year in which it was placed in service.

(3) Property predominantly used in qualified business use

For purposes of this subsection, property shall be treated as predominantly used in a qualified business use for any taxable year if the business use percentage for such taxable year exceeds 50 percent.

(c) Treatment of leases

(1) Lessor's deductions not affected

This section shall not apply to any listed property leased or held for leasing by any person regularly engaged in the business of leasing such property.

(2) Lessee's deductions reduced

For purposes of determining the amount allowable as a deduction under this chapter for rentals or other payments under a lease for a period of 30 days or more of listed property,

only the allowable percentage of such payments shall be taken into account.

(3) Allowable percentage

For purposes of paragraph (2), the allowable percentage shall be determined under tables prescribed by the Secretary. Such tables shall be prescribed so that the reduction in the deduction under paragraph (2) is substantially equivalent to the applicable restrictions contained in subsections (a) and (b).

(4) Lease term

In determining the term of any lease for purposes of paragraph (2), the rules of section 168(i)(3)(A) shall apply.

(5) Lessee recapture

Under regulations prescribed by the Secretary, rules similar to the rules of subsection (b)(3) shall apply to any lessee to which paragraph (2) applies.

(d) Definitions and special rules

For purposes of this section—

(1) Coordination with section 179

Any deduction allowable under section 179 with respect to any listed property shall be subject to the limitations of subsections (a) and (b), and the limitation of paragraph (3) of this subsection, in the same manner as if it were a depreciation deduction allowable under section 168.

(2) Subsequent depreciation deductions reduced for deductions allocable to personal use

Solely for purposes of determining the amount of the depreciation deduction for subsequent taxable years, if less than 100 percent of the use of any listed property during any taxable year is use in a trade or business (including the holding for the production of income), all of the use of such property during such taxable year shall be treated as use so described.

(3) Deductions of employee

(A) In general

Any employee use of listed property shall not be treated as use in a trade or business for purposes of determining the amount of any depreciation deduction allowable to the employee (or the amount of any deduction allowable to the employee for rentals or other payments under a lease of listed property) unless such use is for the convenience of the employer and required as a condition of employment.

(B) Employee use

For purposes of subparagraph (A), the term “employee use” means any use in connection with the performance of services as an employee.

(4) Listed property

(A) In general

Except as provided in subparagraph (B), the term “listed property” means—

- (i) any passenger automobile,
- (ii) any other property used as a means of transportation,

- (iii) any property of a type generally used for purposes of entertainment, recreation, or amusement,

- (iv) any computer or peripheral equipment (as defined in section 168(i)(2)(B)),

- (v) any cellular telephone (or other similar telecommunications equipment), and

- (vi) any other property of a type specified by the Secretary by regulations.

(B) Exception for certain computers

The term “listed property” shall not include any computer or peripheral equipment (as so defined) used exclusively at a regular business establishment and owned or leased by the person operating such establishment. For purposes of the preceding sentence, any portion of a dwelling unit shall be treated as a regular business establishment if (and only if) the requirements of section 280A(c)(1) are met with respect to such portion.

(C) Exception for property used in business of transporting persons or property

Except to the extent provided in regulations, clause (ii) of subparagraph (A) shall not apply to any property substantially all of the use of which is in a trade or business of providing to unrelated persons services consisting of the transportation of persons or property for compensation or hire.

(5) Passenger automobile

(A) In general

Except as provided in subparagraph (B), the term “passenger automobile” means any 4-wheeled vehicle—

- (i) which is manufactured primarily for use on public streets, roads, and highways, and

- (ii) which is rated at 6,000 pounds unloaded gross vehicle weight or less.

In the case of a truck or van, clause (ii) shall be applied by substituting “gross vehicle weight” for “unloaded gross vehicle weight”.

(B) Exception for certain vehicles

The term “passenger automobile” shall not include—

- (i) any ambulance, hearse, or combination ambulance-hearse used by the taxpayer directly in a trade or business,

- (ii) any vehicle used by the taxpayer directly in the trade or business of transporting persons or property for compensation or hire, and

- (iii) under regulations, any truck or van.

(6) Business use percentage

(A) In general

The term “business use percentage” means the percentage of the use of any listed property during any taxable year which is a qualified business use.

(B) Qualified business use

Except as provided in subparagraph (C), the term “qualified business use” means any use in a trade or business of the taxpayer.

(C) Exception for certain use by 5-percent owners and related persons**(i) In general**

The term “qualified business use” shall not include—

(I) leasing property to any 5-percent owner or related person,

(II) use of property provided as compensation for the performance of services by a 5-percent owner or related person, or

(III) use of property provided as compensation for the performance of services by any person not described in subclause (II) unless an amount is included in the gross income of such person with respect to such use, and, where required, there was withholding under chapter 24.

(ii) Special rule for aircraft

Clause (i) shall not apply with respect to any aircraft if at least 25 percent of the total use of the aircraft during the taxable year consists of qualified business use not described in clause (i).

(D) Definitions

For purposes of this paragraph—

(i) 5-percent owner

The term “5-percent owner” means any person who is a 5-percent owner with respect to the taxpayer (as defined in section 416(i)(1)(B)(i)).

(ii) Related person

The term “related person” means any person related to the taxpayer (within the meaning of section 267(b)).

(7) Automobile price inflation adjustment**(A) In general**

In the case of any passenger automobile placed in service after 1988, subsection (a) shall be applied by increasing each dollar amount contained in such subsection by the automobile price inflation adjustment for the calendar year in which such automobile is placed in service. Any increase under the preceding sentence shall be rounded to the nearest multiple of \$100 (or if the increase is a multiple of \$50, such increase shall be increased to the next higher multiple of \$100).

(B) Automobile price inflation adjustment

For purposes of this paragraph—

(i) In general

The automobile price inflation adjustment for any calendar year is the percentage (if any) by which—

(I) the CPI automobile component for October of the preceding calendar year, exceeds

(II) the CPI automobile component for October of 1987.

(ii) CPI automobile component

The term “CPI automobile component” means the automobile component of the Consumer Price Index for All Urban Consumers published by the Department of Labor.

(8) Unrecovered basis

For purposes of subsection (a)(2), the term “unrecovered basis” means the adjusted basis of the passenger automobile determined after the application of subsection (a) and as if all use during the recovery period were use in a trade or business (including the holding of property for the production of income).

(9) All taxpayers holding interests in passenger automobile treated as 1 taxpayer

All taxpayers holding interests in any passenger automobile shall be treated as 1 taxpayer for purposes of applying subsection (a) to such automobile, and the limitations of subsection (a) shall be allocated among such taxpayers in proportion to their interests in such automobile.

(10) Special rule for property acquired in non-recognition transactions

For purposes of subsection (a)(2) any property acquired in a nonrecognition transaction shall be treated as a single property originally placed in service in the taxable year in which it was placed in service after being so acquired.

(e) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations with respect to items properly included in, or excluded from, the adjusted basis of any listed property.

(Added Pub. L. 98-369, div. A, title I, §179(a), July 18, 1984, 98 Stat. 713; amended Pub. L. 99-44, §4, May 24, 1985, 99 Stat. 78; Pub. L. 99-514, title II, §201(d)(4), title XVIII, §1812(e)(1)(A), (C), (2)-(5), Oct. 22, 1986, 100 Stat. 2139, 2836, 2837; Pub. L. 100-647, title I, §§1002(a)(10), (b)(2), 1018(u)(3), Nov. 10, 1988, 102 Stat. 3354, 3357, 3590; Pub. L. 101-239, title VII, §7643(a), Dec. 19, 1989, 103 Stat. 2381; Pub. L. 101-508, title XI, §11813(b)(13)(A)-(E), Nov. 5, 1990, 104 Stat. 1388-554, 1388-555; Pub. L. 104-188, title I, §1702(h)(5), Aug. 20, 1996, 110 Stat. 1874; Pub. L. 105-34, title IX, §971(a), Aug. 5, 1997, 111 Stat. 897; Pub. L. 105-206, title VI, §6009(c), July 22, 1998, 112 Stat. 812; Pub. L. 107-147, title VI, §602(b)(1), Mar. 9, 2002, 116 Stat. 59.)

INFLATION ADJUSTED ITEMS FOR CERTAIN
CALENDAR YEARS

For inflation adjustment of certain items in this section, see Revenue Procedures listed in a table below.

AMENDMENTS

2002—Subsec. (a)(1)(C)(iii). Pub. L. 107-147 added cl. (iii).

1998—Subsec. (a)(1)(C)(ii). Pub. L. 105-206 substituted “subparagraphs (A) and (B)” for “subparagraph (A)”.

1997—Subsec. (a)(1)(C). Pub. L. 105-34 added subpar. (C).

1996—Subsec. (a). Pub. L. 104-188 struck out “investment tax credit and” after “amount of” in heading.

1990—Pub. L. 101-508, §11813(b)(13)(E), struck out “investment tax credit and” after “Limitation on” in section catchline.

Subsec. (a)(1). Pub. L. 101-508, §11813(b)(13)(A)(i), redesignated par. (2) as (1) and struck out former par. (1) “Investment tax credit” which read as follows: “The

amount of the credit determined under section 46(a) for any passenger automobile shall not exceed \$675.”

Subsec. (a)(2). Pub. L. 101-508, §11813(b)(13)(A)(i), redesignated par. (3) as (2). Former par. (2) redesignated (1).

Subsec. (a)(2)(B). Pub. L. 101-508, §11813(b)(13)(A)(ii), struck out “the credit determined under section 46(a) or” after “the amount of”.

Subsec. (a)(3). Pub. L. 101-508, §11813(b)(13)(A)(i), redesignated par. (3) as (2).

Subsec. (a)(4). Pub. L. 101-508, §11813(b)(13)(A)(i), struck out par. (4) “Special rule where election of reduced credit in lieu of the basis adjustment” which read as follows: “In the case of any election under section 48(q)(4) with respect to any passenger automobile, the limitation of paragraph (1) applicable to such passenger automobile shall be ¾ of the amount which would be so applicable but for this paragraph.”

Subsec. (b). Pub. L. 101-508, §11813(b)(13)(B), redesignated pars. (2) to (4) as (1) to (3), respectively, and struck out former par. (1) “Investment tax credit” which read as follows: “For purposes of this subtitle, any listed property shall not be treated as section 38 property for any taxable year unless such property is predominantly used in a qualified business use for such taxable year.”

Subsec. (c)(1). Pub. L. 101-508, §11813(b)(13)(C), struck out “credits and” after “Lessors” in heading.

Subsec. (d)(3)(A). Pub. L. 101-508, §11813(b)(13)(D), struck out “the amount of any credit allowable under section 38 to the employee or” after “of determining”.

1989—Subsec. (d)(4)(A)(v), (vi). Pub. L. 101-239 added cl. (v) and redesignated former cl. (v) as (vi).

1988—Subsec. (b)(3)(B)(i). Pub. L. 100-647, §1018(u)(3), substituted “depreciation deductions” for “recovery deductions”.

Subsec. (d)(1). Pub. L. 100-647, §1002(b)(2), substituted “subsections (a) and (b), and the limitation of paragraph (3) of this subsection,” for “subsections (a) and (b)”.

Subsec. (d)(3)(A). Pub. L. 100-647, §1002(a)(10), substituted “depreciation deduction” for “recovery deduction”.

1986—Subsec. (a)(2)(A). Pub. L. 99-514, §201(d)(4)(A)(i), (K), substituted “depreciation deduction” for “recovery deduction” in introductory provisions and substituted cls. (i) to (iv) for former cls. (i) and (ii) which read as follows:

“(i) \$3,200 for the first taxable year in the recovery period, and

“(ii) \$4,800 for each succeeding taxable year in the recovery period.”

Subsec. (a)(2)(B). Pub. L. 99-514, §201(d)(4)(A)(ii), (K), substituted “\$1,475” for “\$4,800” in heading and text of cl. (ii), and “depreciation deduction” for “recovery deduction” in heading and text of cl. (iv).

Subsec. (a)(3)(B). Pub. L. 99-514, §201(d)(4)(K), substituted “depreciation deduction” for “recovery deduction” in two places.

Subsec. (b)(2). Pub. L. 99-514, §201(d)(4)(J), substituted “section 168(g) (relating to alternative depreciation system)” for “the straight line method over the earnings and profits life for such property”.

Subsec. (b)(3)(A). Pub. L. 99-514, §201(d)(4)(B), (K), substituted “depreciation deduction” for “recovery deduction” and “section 168(g) (relating to alternative depreciation system)” for “the straight line method over the earnings and profits life” in closing provisions.

Subsec. (b)(4). Pub. L. 99-514, §201(d)(4)(C), in amending par. (4) generally, struck out heading “Definitions”, redesignated as par. (4) former subpar. (A) heading and text, substituted “For purposes of this section, property” for “Property”, and struck out former subpar. (B) definition of straight line method over earnings and profits life.

Subsec. (c)(4). Pub. L. 99-514, §201(d)(4)(D), substituted “section 168(i)(3)(A)” for “section 168(j)(6)(B)”.

Subsec. (d)(1). Pub. L. 99-514, §201(d)(4)(E), substituted “depreciation deduction” for “recovery deduction”.

Subsec. (d)(2). Pub. L. 99-514, §1812(e)(5), substituted “is use described in” for “is not use described in”.

Pub. L. 99-514, §201(d)(4)(F), substituted “depreciation deduction” for “recovery deduction” and “use in a trade or business (including the holding for the production of income)” for “use described in section 168(c)(1) (defining recovery property)”.

Subsec. (d)(3)(A). Pub. L. 99-514, §1812(e)(2), inserted “(or the amount of any deduction allowable to the employee for rentals or other payments under a lease of listed property)”.

Subsec. (d)(4)(A)(iv). Pub. L. 99-514, §201(d)(4)(G), substituted “section 168(i)(2)(B)” for “section 168(j)(5)(D)”.

Subsec. (d)(4)(B). Pub. L. 99-514, §1812(e)(3), inserted “and owned or leased by the person operating such establishment”.

Subsec. (d)(4)(C). Pub. L. 99-514, §1812(e)(4), added subpar. (C).

Subsec. (d)(5)(A). Pub. L. 99-514, §1812(e)(1)(A), (C), substituted “unloaded gross vehicle weight” for “gross vehicle weight” in cl. (ii) and inserted at end “In the case of a truck or van, clause (ii) shall be applied by substituting ‘gross vehicle weight’ for ‘unloaded gross vehicle weight’.”

Subsec. (d)(8). Pub. L. 99-514, §201(d)(4)(H), amended par. (8) generally. Prior to amendment, par. (8) read as follows: “For purposes of subsection (a)(2), the term ‘unrecovered basis’ means the excess (if any) of—

“(A) the unadjusted basis (as defined in section 168(d)(1)(A)) of the passenger automobile, over

“(B) the amount of the recovery deductions which would have been allowable for taxable years in the recovery period determined after the application of subsection (a) and as if all use during the recovery period were use described in section 168(c)(1).”

Subsec. (d)(10). Pub. L. 99-514, §201(d)(4)(I), struck out “, notwithstanding any regulations prescribed under section 168(f)(7),” after “For purposes of subsection (a)(2)”.

1985—Subsec. (a)(1). Pub. L. 99-44, §4(a)(1), substituted “\$675” for “\$1,000”.

Subsec. (a)(2)(A)(i). Pub. L. 99-44, §4(a)(2)(A), substituted “\$3,200” for “\$4,000”.

Subsec. (a)(2)(A)(ii), (B)(ii). Pub. L. 99-44, §4(a)(2)(B), substituted “\$4,800” for “\$6,000” wherever appearing in text and heading.

Subsec. (d)(7)(A). Pub. L. 99-44, §4(b)(1), inserted “placed in service after 1988” after “passenger automobile”.

Subsec. (d)(7)(B)(i). Pub. L. 99-44, §4(b)(3), struck out last sentence which directed that in the case of calendar year 1984, the automobile price inflation adjustment would be zero.

Subsec. (d)(7)(B)(i)(II). Pub. L. 99-44, §4(b)(2), substituted “1987” for “1983”.

EFFECTIVE DATE OF 2002 AMENDMENT

Amendment by Pub. L. 107-147 applicable to property placed in service after Dec. 31, 2001, see section 602(c) of Pub. L. 107-147, set out as a note under section 30 of this title.

EFFECTIVE DATE OF 1998 AMENDMENT

Amendment by Pub. L. 105-206 effective, except as otherwise provided, as if included in the provisions of the Taxpayer Relief Act of 1997, Pub. L. 105-34, to which such amendment relates, see section 6024 of Pub. L. 105-206, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1997 AMENDMENT

Pub. L. 105-34, title IX, §971(b), Aug. 5, 1997, 111 Stat. 897, as amended by Pub. L. 107-147, title VI, §602(b)(2), Mar. 9, 2002, 116 Stat. 59, provided that: “The amendments made by this section [amending this section] shall apply to property placed in service after the date of enactment of this Act [Aug. 5, 1997].”

EFFECTIVE DATE OF 1996 AMENDMENT

Amendment by Pub. L. 104-188 effective, except as otherwise expressly provided, as if included in the provision of the Revenue Reconciliation Act of 1990, Pub.

L. 101-508, title XI, to which such amendment relates, see section 1702(i) of Pub. L. 104-188, set out as a note under section 38 of this title.

EFFECTIVE DATE OF 1990 AMENDMENT

Amendment by Pub. L. 101-508 applicable to property placed in service after Dec. 31, 1990, but not applicable to any transition property (as defined in section 49(e) of this title), any property with respect to which qualified progress expenditures were previously taken into account under section 46(d) of this title, and any property described in section 46(b)(2)(C) of this title, as such sections were in effect on Nov. 4, 1990, see section 11813(c) of Pub. L. 101-508, set out as a note under section 45K of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Section 7643(b) of Pub. L. 101-239 provided that: “The amendment made by subsection (a) [amending this section] shall apply to property placed in service or leased in taxable years beginning after December 31, 1989.”

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 201(d)(4) of Pub. L. 99-514 applicable to property placed in service after Dec. 31, 1986, in taxable years ending after such date, with exceptions, see sections 203 and 204 of Pub. L. 99-514, set out as a note under section 168 of this title.

Amendment by section 201(d)(4) of Pub. L. 99-514 not applicable to any property placed in service before Jan. 1, 1994, if such property placed in service as part of specified rehabilitations, and not applicable to certain additional rehabilitations, see section 251(d)(2), (3) of Pub. L. 99-514, set out as a note under section 46 of this title.

Amendment by section 1812(e)(1)(A), (C), (2)-(5) of Pub. L. 99-514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98-369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99-514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1985 AMENDMENT

Section 6(e) of Pub. L. 99-44 provided that: “(1) Except as provided in paragraph (2), the amendments made by section 4 [amending this section] shall apply to—

“(A) property placed in service after April 2, 1985, in taxable years ending after such date, and

“(B) property leased after April 2, 1985, in taxable years ending after such date.

“(2) The amendments made by section 4 [amending this section] shall not apply to any property—

“(A) acquired by the taxpayer pursuant to a binding contract in effect on April 1, 1985, and at all times thereafter, but only if the property is placed in service before August 1, 1985, or

“(B) of which the taxpayer is the lessee, but only if the lease is pursuant to a binding contract in effect on April 1, 1985, and at all times thereafter, and only if the taxpayer first uses such property under the lease before August 1, 1985.”

EFFECTIVE DATE

Section 179(d) of Pub. L. 98-369 provided that:

“(1) IN GENERAL.—

“(A) Except as provided in subparagraph (B), the amendments made by subsections (a) and (c) [enacting this section] shall apply to—

“(i) property placed in service after June 18, 1984, in taxable years ending after such date, and

“(ii) property leased after June 18, 1984, in taxable years ending after such date.

“(B) The amendments made by subsections (a) and (c) shall not apply to any property—

“(i) acquired by the taxpayer pursuant to a binding contract in effect on June 18, 1984, and at all times thereafter (or under construction on such date) but only if the property is placed in service before January 1, 1985 (January 1, 1987, in the case of 15-year real property), or

“(ii) of which the taxpayer is the lessee but only if the lease is pursuant to a binding contract in effect on June 18, 1984, and at all times thereafter and only if the taxpayer first uses such property under the lease before January 1, 1985 (January 1, 1987, in the case of 15-year real property).

For purposes of the preceding sentence, the term ‘15-year real property’ includes 18-year real property.

“(2) COMPLIANCE PROVISIONS.—The amendments made by subsection (b) [amending sections 274, 6653, and 6695 of this title] shall apply to taxable years beginning after December 31, 1984.”

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101-508 be construed to affect treatment of certain transactions occurring, property acquired, or items of income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101-508, set out as a note under section 45K of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL
JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§1101-1147 and 1171-1177] or title XVIII [§§1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

INFLATION ADJUSTED ITEMS FOR CERTAIN CALENDAR
YEARS

Provisions relating to inflation adjustment of items in this section for certain calendar years were contained in the following:

- 2009—Revenue Procedure 2009-24.
- 2008—Revenue Procedure 2008-22.
- 2007—Revenue Procedure 2007-30.
- 2006—Revenue Procedure 2006-18.
- 2005—Revenue Procedure 2005-13.
- 2004—Revenue Procedure 2004-20.
- 2003—Revenue Procedure 2003-75.
- 2002—Revenue Procedure 2002-14.
- 2001—Revenue Procedure 2001-19.
- 2000—Revenue Procedure 2000-18.
- 1999—Revenue Procedure 99-14.
- 1998—Revenue Procedures 98-24 and 98-30.
- 1997—Revenue Procedure 97-20.
- 1996—Revenue Procedure 96-25.

§ 280G. Golden parachute payments

(a) General rule

No deduction shall be allowed under this chapter for any excess parachute payment.

(b) Excess parachute payment

For purposes of this section—

(1) In general

The term “excess parachute payment” means an amount equal to the excess of any parachute payment over the portion of the base amount allocated to such payment.

(2) Parachute payment defined**(A) In general**

The term “parachute payment” means any payment in the nature of compensation to (or for the benefit of) a disqualified individual if—

(i) such payment is contingent on a change—

(I) in the ownership or effective control of the corporation, or

(II) in the ownership of a substantial portion of the assets of the corporation, and

(ii) the aggregate present value of the payments in the nature of compensation to (or for the benefit of) such individual which are contingent on such change equals or exceeds an amount equal to 3 times the base amount.

For purposes of clause (ii), payments not treated as parachute payments under paragraph (4)(A), (5), or (6) shall not be taken into account.

(B) Agreements

The term “parachute payment” shall also include any payment in the nature of compensation to (or for the benefit of) a disqualified individual if such payment is made pursuant to an agreement which violates any generally enforced securities laws or regulations. In any proceeding involving the issue of whether any payment made to a disqualified individual is a parachute payment on account of a violation of any generally enforced securities laws or regulations, the burden of proof with respect to establishing the occurrence of a violation of such a law or regulation shall be upon the Secretary.

(C) Treatment of certain agreements entered into within 1 year before change of ownership

For purposes of subparagraph (A)(i), any payment pursuant to—

(i) an agreement entered into within 1 year before the change described in subparagraph (A)(i), or

(ii) an amendment made within such 1-year period of a previous agreement,

shall be presumed to be contingent on such change unless the contrary is established by clear and convincing evidence.

(3) Base amount**(A) In general**

The term “base amount” means the individual’s annualized includible compensation for the base period.

(B) Allocation

The portion of the base amount allocated to any parachute payment shall be an amount which bears the same ratio to the base amount as—

(i) the present value of such payment, bears to

(ii) the aggregate present value of all such payments.

(4) Treatment of amounts which taxpayer establishes as reasonable compensation

In the case of any payment described in paragraph (2)(A)—

(A) the amount treated as a parachute payment shall not include the portion of such payment which the taxpayer establishes by clear and convincing evidence is reasonable compensation for personal services to be rendered on or after the date of the change described in paragraph (2)(A)(i), and

(B) the amount treated as an excess parachute payment shall be reduced by the portion of such payment which the taxpayer establishes by clear and convincing evidence is reasonable compensation for personal services actually rendered before the date of the change described in paragraph (2)(A)(i).

For purposes of subparagraph (B), reasonable compensation for services actually rendered before the date of the change described in paragraph (2)(A)(i) shall be first offset against the base amount.

(5) Exemption for small business corporations, etc.**(A) In general**

Notwithstanding paragraph (2), the term “parachute payment” does not include—

(i) any payment to a disqualified individual with respect to a corporation which (immediately before the change described in paragraph (2)(A)(i)) was a small business corporation (as defined in section 1361(b) but without regard to paragraph (1)(C) thereof), and

(ii) any payment to a disqualified individual with respect to a corporation (other than a corporation described in clause (i)) if—

(I) immediately before the change described in paragraph (2)(A)(i), no stock in such corporation was readily tradeable on an established securities market or otherwise, and

(II) the shareholder approval requirements of subparagraph (B) are met with respect to such payment.

The Secretary may, by regulations, prescribe that the requirements of subclause (I) of clause (ii) are not met where a substantial portion of the assets of any entity consists (directly or indirectly) of stock in such corporation and interests in such other entity are readily tradeable on an established securities market, or otherwise. Stock described in section 1504(a)(4) shall not be taken into account under clause (ii)(I) if the payment does not adversely affect the shareholder’s redemption and liquidation rights.

(B) Shareholder approval requirements

The shareholder approval requirements of this subparagraph are met with respect to any payment if—

(i) such payment was approved by a vote of the persons who owned, immediately before the change described in paragraph (2)(A)(i), more than 75 percent of the vot-

ing power of all outstanding stock of the corporation, and

(ii) there was adequate disclosure to shareholders of all material facts concerning all payments which (but for this paragraph) would be parachute payments with respect to a disqualified individual.

The regulations prescribed under subsection (e) shall include regulations providing for the application of this subparagraph in the case of shareholders which are not individuals (including the treatment of nonvoting interests in an entity which is a shareholder) and where an entity holds a de minimis amount of stock in the corporation.

(6) Exemption for payments under qualified plans

Notwithstanding paragraph (2), the term “parachute payment” shall not include any payment to or from—

(A) a plan described in section 401(a) which includes a trust exempt from tax under section 501(a),

(B) an annuity plan described in section 403(a),

(C) a simplified employee pension (as defined in section 408(k)), or

(D) a simple retirement account described in section 408(p).

(c) Disqualified individuals

For purposes of this section, the term “disqualified individual” means any individual who is—

(1) an employee, independent contractor, or other person specified in regulations by the Secretary who performs personal services for any corporation, and

(2) is an officer, shareholder, or highly-compensated individual.

For purposes of this section, a personal service corporation (or similar entity) shall be treated as an individual. For purposes of paragraph (2), the term “highly-compensated individual” only includes an individual who is (or would be if the individual were an employee) a member of the group consisting of the highest paid 1 percent of the employees of the corporation or, if less, the highest paid 250 employees of the corporation.

(d) Other definitions and special rules

For purposes of this section—

(1) Annualized includible compensation for base period

The term “annualized includible compensation for the base period” means the average annual compensation which—

(A) was payable by the corporation with respect to which the change in ownership or control described in paragraph (2)(A) of subsection (b) occurs, and

(B) was includible in the gross income of the disqualified individual for taxable years in the base period.

(2) Base period

The term “base period” means the period consisting of the most recent 5 taxable years ending before the date on which the change in ownership or control described in paragraph

(2)(A) of subsection (b) occurs (or such portion of such period during which the disqualified individual performed personal services for the corporation).

(3) Property transfers

Any transfer of property—

(A) shall be treated as a payment, and

(B) shall be taken into account as its fair market value.

(4) Present value

Present value shall be determined by using a discount rate equal to 120 percent of the applicable Federal rate (determined under section 1274(d)), compounded semiannually.

(5) Treatment of affiliated groups

Except as otherwise provided in regulations, all members of the same affiliated group (as defined in section 1504, determined without regard to section 1504(b)) shall be treated as 1 corporation for purposes of this section. Any person who is an officer of any member of such group shall be treated as an officer of such 1 corporation.

(e) Special rule for application to employers participating in the Troubled Assets Relief Program

(1) In general

In the case of the severance from employment of a covered executive of an applicable employer during the period during which the authorities under section 101(a) of the Emergency Economic Stabilization Act of 2008 are in effect (determined under section 120 of such Act), this section shall be applied to payments to such executive with the following modifications:

(A) Any reference to a disqualified individual (other than in subsection (c)) shall be treated as a reference to a covered executive.

(B) Any reference to a change described in subsection (b)(2)(A)(i) shall be treated as a reference to an applicable severance from employment of a covered executive, and any reference to a payment contingent on such a change shall be treated as a reference to any payment made during an applicable taxable year of the employer on account of such applicable severance from employment.

(C) Any reference to a corporation shall be treated as a reference to an applicable employer.

(D) The provisions of subsections (b)(2)(C), (b)(4), (b)(5), and (d)(5) shall not apply.

(2) Definitions and special rules

For purposes of this subsection:

(A) Definitions

Any term used in this subsection which is also used in section 162(m)(5) shall have the meaning given such term by such section.

(B) Applicable severance from employment

The term “applicable severance from employment” means any severance from employment of a covered executive—

(i) by reason of an involuntary termination of the executive by the employer, or

(ii) in connection with any bankruptcy, liquidation, or receivership of the employer.

(C) Coordination and other rules

(i) In general

If a payment which is treated as a parachute payment by reason of this subsection is also a parachute payment determined without regard to this subsection, this subsection shall not apply to such payment.

(ii) Regulatory authority

The Secretary may prescribe such guidance, rules, or regulations as are necessary—

(I) to carry out the purposes of this subsection and the Emergency Economic Stabilization Act of 2008, including the extent to which this subsection applies in the case of any acquisition, merger, or reorganization of an applicable employer,

(II) to apply this section and section 4999 in cases where one or more payments with respect to any individual are treated as parachute payments by reason of this subsection, and other payments with respect to such individual are treated as parachute payments under this section without regard to this subsection, and

(III) to prevent the avoidance of the application of this section through the mischaracterization of a severance from employment as other than an applicable severance from employment.

(f) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section (including regulations for the application of this section in the case of related corporations and in the case of personal service corporations).

(Added Pub. L. 98-369, div. A, title I, § 67(a), July 18, 1984, 98 Stat. 585; amended Pub. L. 99-121, title I, § 102(c)(4), Oct. 11, 1985, 99 Stat. 508; Pub. L. 99-514, title XVIII, § 1804(j), Oct. 22, 1986, 100 Stat. 2807; Pub. L. 100-647, title I, § 1018(d)(6)-(8), Nov. 10, 1988, 102 Stat. 3581; Pub. L. 104-188, title I, § 1421(b)(9)(A), Aug. 20, 1996, 110 Stat. 1798; Pub. L. 110-343, div. A, title III, § 302(b), Oct. 3, 2008, 122 Stat. 3805.)

REFERENCES IN TEXT

The Emergency Economic Stabilization Act of 2008, referred to in subsec. (e)(1), (2)(C)(ii)(I), is Pub. L. 110-343, div. A, Oct. 3, 2008, 122 Stat. 3765. Section 101(a) of the Act enacted section 5211(a) of Title 12, Banks and Banking, and amended section 5315 of Title 5, Government Organization and Employees, and section 301 of Title 31, Money and Finance. Section 120 of the Act is classified to section 5230 of Title 12. For complete classification of this Act to the Code, see Short Title note set out under section 5201 of Title 12 and Tables.

AMENDMENTS

2008—Subsecs. (e), (f). Pub. L. 110-343 added subsec. (e) and redesignated former subsec. (e) as (f).

1996—Subsec. (b)(6)(D). Pub. L. 104-188 added subpar. (D).

1988—Subsec. (b)(5)(A). Pub. L. 100-647, § 1018(d)(6), substituted “section 1361(b) but without regard to paragraph (1)(C) thereof” for “section 1361(b)” in cl. (i) and inserted at end “Stock described in section 1504(a)(4) shall not be taken into account under clause (ii)(I) if the payment does not adversely affect the shareholder’s redemption and liquidation rights.”

Subsec. (b)(5)(B). Pub. L. 100-647, § 1018(d)(7), inserted at end “The regulations prescribed under subsection (e) shall include regulations providing for the application of this subparagraph in the case of shareholders which are not individuals (including the treatment of non-voting interests in an entity which is a shareholder) and where an entity holds a de minimis amount of stock in the corporation.”

Subsec. (d)(5). Pub. L. 100-647, § 1018(d)(8), substituted “officer of any member” for “officer or any member”.

1986—Subsec. (b)(2)(A). Pub. L. 99-514, § 1804(j)(6), inserted “For purposes of clause (ii), payments not treated as parachute payments under paragraph (4)(A), (5), or (6) shall not be taken into account.”

Subsec. (b)(2)(B). Pub. L. 99-514, § 1804(j)(7), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: “The term ‘parachute payment’ shall also include any payment in the nature of compensation to (or for the benefit of) a disqualified individual if such payment is pursuant to an agreement which violates any securities laws or regulations.”

Subsec. (b)(4). Pub. L. 99-514, § 1804(j)(2), substituted “Treatment of amounts which taxpayer establishes as reasonable compensation” for “Excess parachute payments reduced to extent taxpayer establishes reasonable compensation” in heading and amended text generally. Prior to amendment, text read as follows: “In the case of any parachute payment described in paragraph (2)(A), the amount of any excess parachute payment shall be reduced by the portion of such payment which the taxpayer establishes by clear and convincing evidence is reasonable compensation for personal services actually rendered. For purposes of the preceding sentence, reasonable compensation shall be first offset against the base amount.”

Subsec. (b)(5). Pub. L. 99-514, § 1804(j)(1), added par. (5).

Subsec. (b)(6). Pub. L. 99-514, § 1804(j)(3), added par. (6).

Subsec. (c). Pub. L. 99-514, § 1804(j)(5), inserted provision defining “highly-compensated individual”.

Subsec. (d)(2). Pub. L. 99-514, § 1804(j)(8), substituted “performed personal services for the corporation” for “was an employee of the corporation”.

Subsec. (d)(5). Pub. L. 99-514, § 1804(j)(4), added par. (5).

EFFECTIVE DATE OF 2008 AMENDMENT

Pub. L. 110-343, div. A, title III, § 302(c)(2), Oct. 3, 2008, 122 Stat. 3806, provided that: “The amendments made by subsection (b) [amending this section] shall apply to payments with respect to severances occurring during the period during which the authorities under section 101(a) of this Act [enacting section 5211(a) of Title 12, Banks and Banking, and amending section 5315 of Title 5, Government Organization and Employees, and section 301 of Title 31, Money and Finance] are in effect (determined under section 120 of this Act [12 U.S.C. 5230]).”

EFFECTIVE DATE OF 1996 AMENDMENT

Amendment by Pub. L. 104-188 applicable to taxable years beginning after Dec. 31, 1996, see section 1421(e) of Pub. L. 104-188, set out as a note under section 72 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99-514, to which such amendment relates, see section 1019(a) of Pub. L. 100-647, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by Pub. L. 99-514 effective, except as otherwise provided, as if included in the provisions of the Tax Reform Act of 1984, Pub. L. 98-369, div. A, to which such amendment relates, see section 1881 of Pub. L. 99-514, set out as a note under section 48 of this title.

EFFECTIVE DATE OF 1985 AMENDMENT

Amendment by Pub. L. 99-121 applicable to sales and exchanges after June 30, 1985, in taxable years ending after such date, see section 105(a)(1) of Pub. L. 99-121, set out as a note under section 1274 of this title.

EFFECTIVE DATE

Section 67(e) of Pub. L. 98-369 provided that:

“(1) IN GENERAL.—The amendments made by this section [enacting this section and section 4999 of this title and amending sections 275 and 3121 of this title] shall apply to payments under agreements entered into or renewed after June 14, 1984, in taxable years ending after such date.

“(2) SPECIAL RULE FOR CONTRACT AMENDMENTS.—Any contract entered into before June 15, 1984, which is amended after June 14, 1984, in any significant relevant aspect shall be treated as a contract entered into after June 14, 1984.”

PLAN AMENDMENTS NOT REQUIRED UNTIL
JANUARY 1, 1998

For provisions directing that if any amendments made by subtitle D [§§1401-1465] of title I of Pub. L. 104-188 require an amendment to any plan or annuity contract, such amendment shall not be required to be made before the first day of the first plan year beginning on or after Jan. 1, 1998, see section 1465 of Pub. L. 104-188, set out as a note under section 401 of this title.

PLAN AMENDMENTS NOT REQUIRED UNTIL
JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§1101-1147 and 1171-1177] or title XVIII [§§1800-1899A] of Pub. L. 99-514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99-514, as amended, set out as a note under section 401 of this title.

§ 280H. Limitation on certain amounts paid to employee-owners by personal service corporations electing alternative taxable years

(a) General rule

If—

(1) an election by a personal service corporation under section 444 is in effect for a taxable year, and

(2) such corporation does not meet the minimum distribution requirements of subsection (c) for such taxable year,

then the deduction otherwise allowed under this chapter for applicable amounts paid or incurred by such corporation to employee-owners shall not exceed the maximum deductible amount. The preceding sentence shall not apply for purposes of subchapter G (relating to personal holding companies).

(b) Carryover of nondeductible amounts

If any amount is not allowed as a deduction for a taxable year under subsection (a), such amount shall be treated as paid or incurred in the succeeding taxable year.

(c) Minimum distribution requirement

For purposes of this section—

(1) In general

A personal service corporation meets the minimum distribution requirements of this subsection if the applicable amounts paid or incurred during the deferral period of the taxable year (determined without regard to subsection (b)) equal or exceed the lesser of—

(A) the product of—

(i) the applicable amounts paid during the preceding taxable year, divided by the number of months in such taxable year, multiplied by

(ii) the number of months in the deferral period of the preceding taxable year, or

(B) the applicable percentage of the adjusted taxable income for the deferral period of the taxable year.

(2) Applicable percentage

The term “applicable percentage” means the percentage (not in excess of 95 percent) determined by dividing—

(A) the applicable amounts paid or incurred during the 3 taxable years immediately preceding the taxable year, by

(B) the adjusted taxable income of such corporation for such 3 taxable years.

(d) Maximum deductible amount

For purposes of this section, the term “maximum deductible amount” means the sum of—

(1) the applicable amounts paid during the deferral period, plus

(2) an amount equal to the product of—

(A) the amount determined under paragraph (1), divided by the number of months in the deferral period, multiplied by

(B) the number of months in the nondeferral period.

(e) Disallowance of net operating loss carrybacks

No net operating loss carryback shall be allowed to (or from) any taxable year of a personal service corporation to which an election under section 444 applies.

(f) Other definitions and special rules

For purposes of this section—

(1) Applicable amount

The term “applicable amount” means any amount paid to an employee-owner which is includible in the gross income of such employee, other than—

(A) any gain from the sale or exchange of property between the owner-employee and the corporation, or

(B) any dividend paid by the corporation.

(2) Employee-owner

The term “employee-owner” has the meaning given such term by section 269A(b)(2) (as modified by section 441(i)(2)).

(3) Nondeferral and deferral periods**(A) Deferral period**

The term “deferral period” has the meaning given to such term by section 444(b)(4).

(B) Nondeferral period

The term “nondeferral period” means the portion of the taxable year of the personal service corporation which occurs after the

portion of such year constituting the deferral period.

(4) Adjusted taxable income

The term “adjusted taxable income” means taxable income determined without regard to—

(A) any amount paid to an employee-owner which is includible in the gross income of such employee-owner, and

(B) any net operating loss carryover to the extent such carryover is attributable to amounts described in subparagraph (A).

(5) Personal service corporation

The term “personal service corporation” has the meaning given to such term by section 441(i)(2).

(Added Pub. L. 100-203, title X, §10206(c)(1), Dec. 22, 1987, 101 Stat. 1330-401; amended Pub. L. 100-647, title II, §2004(e)(2)(B), (3), (14)(A), (C), Nov. 10, 1988, 102 Stat. 3600, 3602.)

AMENDMENTS

1988—Subsecs. (c)(1)(A)(i), (d)(1). Pub. L. 100-647, §2004(e)(14)(C), substituted “amounts paid” for “amounts paid or incurred”.

Subsec. (f)(2). Pub. L. 100-647, §2004(e)(3), substituted “section 269A(b)(2) (as modified by section 441(i)(2))” for “section 296A(b)(2)”.

Subsec. (f)(4). Pub. L. 100-647, §2004(e)(14)(A), amended par. (4) generally. Prior to amendment, par. (4) read as follows: “The term ‘adjusted taxable income’ means taxable income increased by any amount paid or incurred to an employee-owner which was includible in the gross income of such employee-owner.”

Subsec. (f)(5). Pub. L. 100-647, §2004(e)(2)(B), added par. (5).

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by Pub. L. 100-647 effective, except as otherwise provided, as if included in the provisions of the Revenue Act of 1987, Pub. L. 100-203, title X, to which such amendment relates, see section 2004(u) of Pub. L. 100-647, set out as a note under section 56 of this title.

EFFECTIVE DATE

Section applicable to taxable years beginning after Dec. 31, 1986, see section 10206(d)(1) of Pub. L. 100-203, set out as a note under section 444 of this title.

PART X—TERMINAL RAILROAD CORPORATIONS AND THEIR SHAREHOLDERS

Sec.

281. Terminal railroad corporations and their shareholders.

AMENDMENTS

1962—Pub. L. 87-870, §1(a), Oct. 23, 1962, 76 Stat. 1158, added part X and item 281.

§ 281. Terminal railroad corporations and their shareholders

(a) Computation of taxable income of terminal railroad corporations

(1) In general

In computing the taxable income of a terminal railroad corporation—

(A) such corporation shall not be considered to have received or accrued—

(i) the portion of any liability of any railroad corporation, with respect to relat-

ed terminal services provided by such corporation, which is discharged by crediting such liability with an amount of related terminal income, or

(ii) the portion of any charge which would be made by such corporation for related terminal services provided by it, but which is not made as a result of taking related terminal income into account in computing such charge; and

(B) no deduction otherwise allowable under this chapter shall be disallowed as a result of any discharge of liability described in subparagraph (A)(i) or as a result of any computation of charges in the manner described in subparagraph (A)(ii).

(2) Limitation

In the case of any taxable year ending after the date of the enactment of this section, paragraph (1) shall not apply to the extent that it would (but for this paragraph) operate to create (or increase) a net operating loss for the terminal railroad corporation for the taxable year.

(b) Computation of taxable income of shareholders

Subject to the limitation in subsection (a)(2), in computing the taxable income of any shareholder of a terminal railroad corporation, no amount shall be considered to have been received or accrued or paid or incurred by such shareholder as a result of any discharge of liability described in subsection (a)(1)(A)(i) or as a result of any computation of charges in the manner described in subsection (a)(1)(A)(ii).

(c) Agreement required

In the case of any taxable year, subsections (a) and (b) shall apply with respect to any discharge of liability described in subsection (a)(1)(A)(i), and to any computation of charges in the manner described in subsection (a)(1)(A)(ii), only if such discharge or computation (as in the case may be) was provided for in a written agreement, to which all of the shareholders of the terminal railroad corporation were parties, entered into before the beginning of such taxable year.

(d) Definitions

For purposes of this section—

(1) Terminal railroad corporation

The term “terminal railroad corporation” means a domestic railroad corporation which is not a member, other than as a common parent corporation, of an affiliated group (as defined in section 1504) and—

(A) all of the shareholders of which are rail carriers subject to part A of subtitle IV of title 49;

(B) the primary business of which is the providing of railroad terminal and switching facilities and services to rail carriers subject to part A of subtitle IV of title 49 and to the shippers and passengers of such railroad corporations;

(C) a substantial part of the services of which for the taxable year is rendered to one or more of its shareholders; and

(D) each shareholder of which computes its taxable income on the basis of a taxable