

§1.263A-11) with respect to noninventory property only to the extent those costs were required to be capitalized under section 263 when incurred and would have been taken into account in determining the amount of interest required to be capitalized under former section 189 (relating to the capitalization of real property interest and taxes) or pursuant to an election that was in effect under section 266 (relating to the election to capitalize certain carrying charges).

(2) *Property used to produce designated property.* The basis of property acquired prior to 1987 and used to produce designated noninventory property after December 31, 1986, is included in accumulated production expenditures in accordance with §1.263A-11(d) without regard to whether the basis would have been taken into account under former section 189 or section 266.

(c) *Anti-abuse rule.* The interest capitalization rules contained in §§1.263A-8 through 1.263A-15 must be applied by the taxpayer in a manner that is consistent with and reasonably carries out the purposes of section 263A(f). For example, in applying §1.263A-10, regarding the definition of a unit of property, taxpayers may not divide a single unit of property to avoid property classifying the property as designated property. Similarly, taxpayers may not use loans in lieu of advance payments, tax-exempt parties, loan restructurings at measurement dates, or obligations bearing an unreasonably low rate of interest (even if such rate equals or exceeds the applicable Federal rate under section 1274(d)) to avoid the purposes of section 263A(f). For purposes of this paragraph (c), the presence of back-to-back loans with different rates of interest, and other uses of related parties to facilitate an avoidance of interest capitalization, evidences abuse. In such cases, the District Director may, based upon all the facts and circumstances, determine the amount of interest that must be capitalized in a manner that is consistent with and reasonably carries out the purposes of section 263A(f).

[T.D. 8584, 59 FR 67215, Dec. 29, 1994, as amended by T.D. 8728, 62 FR 42062, Aug. 5, 1997]

**§ 1.264-1 Premiums on life insurance taken out in a trade or business.**

(a) *When premiums are not deductible.* Premiums paid by a taxpayer on a life insurance policy are not deductible from the taxpayer's gross income, even though they would otherwise be deductible as trade or business expenses, if they are paid on a life insurance policy covering the life of any officer or employee of the taxpayer, or any person (including the taxpayer) who is financially interested in any trade or business carried on by the taxpayer, when the taxpayer is directly or indirectly a beneficiary of the policy. For additional provisions relating to the nondeductibility of premiums paid on life insurance policies (whether under section 162 or any other section of the Code), see section 262, relating to personal, living, and family expenses, and section 265, relating to expenses allocable to tax-exempt income.

(b) *When taxpayer is a beneficiary.* If a taxpayer takes out a policy for the purpose of protecting himself from loss in the event of the death of the insured, the taxpayer is considered a beneficiary directly or indirectly under the policy. However, if the taxpayer is not a beneficiary under the policy, the premiums so paid will not be disallowed as deductions merely because the taxpayer may derive a benefit from the increased efficiency of the officer or employee insured. See section 162 and the regulations thereunder. A taxpayer is considered a beneficiary under a policy where, for example, he, as a principal member of a partnership, takes out an insurance policy on his own life irrevocably designating his partner as the sole beneficiary in order to induce his partner to retain his investment in the partnership. Whether or not the taxpayer is a beneficiary under a policy, the proceeds of the policy paid by reason of the death of the insured may be excluded from gross income whether the beneficiary is an individual or a corporation, except in the case of (1) certain transferees, as provided in section 101(a)(2); (2) portions of amounts of life insurance proceeds received at a

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date later than death under the provisions of section 101(d); and (3) life insurance policy proceeds which are includible in the gross income of a husband or wife under section 71 (relating to alimony) or section 682 (relating to income of an estate or trust in case of divorce, etc.). (See section 101(e).) For further reference, see, generally, section 101 and the regulations thereunder.

**§ 1.264-2 Single premium life insurance, endowment, or annuity contracts.**

Amounts paid or accrued on indebtedness incurred or continued, directly or indirectly, to purchase or to continue in effect a single premium life insurance or endowment contract, or to purchase or to continue in effect a single premium annuity contract purchased (whether from the insurer, annuitant, or any other person) after March 1, 1954, are not deductible under section 163 or any other provision of chapter 1 of the Code. This prohibition applies even though the insurance is not on the life of the taxpayer and regardless of whether or not the taxpayer is the annuitant or payee of such annuity contract. A contract is considered a single premium life insurance, endowment, or annuity contract, for the purposes of this section, if substantially all the premiums on the contract are paid within four years from the date on which the contract was purchased, or if an amount is deposited after March 1, 1954, with the insurer for payment of a substantial number of future premiums on the contract.

**§ 1.264-3 Effective date; taxable years ending after March 1, 1954, subject to the Internal Revenue Code of 1939.**

Pursuant to section 7851(a)(1)(C), the regulations prescribed in § 1.264-2, to the extent that they relate to amounts paid or accrued on indebtedness incurred or continued to purchase or carry a single premium annuity contract purchased after March 1, 1954, and to the extent they consider a contract a single premium life insurance, endowment, or annuity contract if an amount is deposited after March 1, 1954, with the insurer for payment of a substantial number of future premiums

on the contract, shall also apply to taxable years beginning before January 1, 1954, and ending after March 1, 1954, and to taxable years beginning after December 31, 1953, and ending after March 1, 1954, but before August 17, 1954, although such years are subject to the Internal Revenue Code of 1939.

**§ 1.264-4 Other life insurance, endowment, or annuity contracts.**

(a) *General rule.* Except as otherwise provided in paragraphs (d) and (e) of this section, no deduction shall be allowed under section 163 or any other provision of chapter 1 of the Code for any amount (determined under paragraph (b) of this section) paid or accrued during the taxable year on indebtedness incurred or continued to purchase or continue in effect a life insurance, endowment, or annuity contract (other than a single premium contract or a contract treated as a single premium contract) if such indebtedness is incurred 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). For the purposes of the preceding sentence, the term of *purchase* includes the payment of part or all of the premiums on a contract, and not merely payment of the premium due upon initial issuance of the contract. The rule of this paragraph applies whether or not the taxpayer is the insured, payee, or annuitant under the contract. The rule of this paragraph does not apply to contracts purchased by the taxpayer on or before August 6, 1963, even though there is a substantial increase in premiums after such date. The rule of this paragraph does not apply to any amount paid or accrued on indebtedness incurred or continued to purchase or carry a single premium life insurance, endowment, or annuity contract (including a contract treated as a single premium contract); the treatment of such amounts is governed by § 1.264-2.

(b) *Determination of amount not allowed.* The amount not allowed as a deduction under paragraph (a) of this section is determined with reference to the entire amount of borrowing to purchase or carry the contract, and is not