

X may deduct the entire amount of the organizational expenditures in 2011, the taxable year in which Corporation X begins business.

Example 2. Expenditures of more than \$5,000 but less than or equal to \$50,000. The facts are the same as in *Example 1* except that Corporation X incurs organizational expenditures of \$41,000. Under paragraph (c) of this section, Corporation X is deemed to have elected to amortize organizational expenditures under section 248(a) in 2011. Therefore, Corporation X may deduct \$5,000 and the portion of the remaining \$36,000 that is allocable to July through December of 2011 ($\$36,000/180 \times 6 = \$1,200$) in 2011, the taxable year in which Corporation X begins business. Corporation X may amortize the remaining \$34,800 ($\$36,000 - \$1,200 = \$34,800$) ratably over the remaining 174 months.

Example 3. Subsequent change in the characterization of an item. The facts are the same as in *Example 2* except that Corporation X determines in 2013 that Corporation X incurred \$10,000 for an additional organizational expenditure erroneously deducted in 2011 under section 162 as a business expense. Under paragraph (c) of this section, Corporation X is deemed to have elected to amortize organizational expenditures under section 248(a) in 2011, including the additional \$10,000 of organizational expenditures. Corporation X is using an impermissible method of accounting for the additional \$10,000 of organizational expenditures and must change its method under § 1.446-1(e) and the applicable general administrative procedures in effect in 2013.

Example 4. Subsequent redetermination of year in which business begins. The facts are the same as in *Example 2* except that, in 2012, Corporation X deducted the organizational expenditures allocable to January through December of 2012 ($\$36,000/180 \times 12 = \$2,400$). In addition, in 2013 it is determined that Corporation X actually began business in 2012. Under paragraph (c) of this section, Corporation X is deemed to have elected to amortize organizational expenditures under section 248(a) in 2012. Corporation X impermissibly deducted organizational expenditures in 2011, and incorrectly determined the amount of organizational expenditures deducted in 2012. Therefore, Corporation X is using an impermissible method of accounting for the organizational expenditures and must change its method under § 1.446-1(e) and the applicable general administrative procedures in effect in 2013.

Example 5. Expenditures of more than \$50,000 but less than or equal to \$55,000. The facts are the same as in *Example 1* except that Corporation X incurs organizational expenditures of \$54,500. Under paragraph (c) of this section, Corporation X is deemed to have elected to amortize organizational expenditures under section 248(a) in 2011. Therefore, Corporation X may deduct \$500 ($\$5,000 -$

$\$4,500$) and the portion of the remaining \$54,000 that is allocable to July through December of 2011 ($\$54,000/180 \times 6 = \$1,800$) in 2011, the taxable year in which Corporation X begins business. Corporation X may amortize the remaining \$52,200 ($\$54,000 - \$1,800 = \$52,200$) ratably over the remaining 174 months.

Example 6. Expenditures of more than \$55,000. The facts are the same as in *Example 1* except that Corporation X incurs organizational expenditures of \$450,000. Under paragraph (c) of this section, Corporation X is deemed to have elected to amortize organizational expenditures under section 248(a) in 2011. Therefore, Corporation X may deduct the amounts allocable to July through December of 2011 ($\$450,000/180 \times 6 = \$15,000$) in 2011, the taxable year in which Corporation X begins business. Corporation X may amortize the remaining \$435,000 ($\$450,000 - \$15,000 = \$435,000$) ratably over the remaining 174 months.

(f) *Effective/applicability date.* This section applies to organizational expenditures paid or incurred after August 16, 2011. However, taxpayers may apply all the provisions of this section to organizational expenditures paid or incurred after October 22, 2004, provided that the period of limitations on assessment of tax for the year the election under paragraph (c) of this section is deemed made has not expired. For organizational expenditures paid or incurred on or before September 8, 2008, taxpayers may instead apply § 1.248-1, as in effect prior to that date (§ 1.248-1 as contained in 26 CFR part 1 edition revised as of April 1, 2008).

[T.D. 9411, 73 FR 38913, July 8, 2008, as amended by T.D. 9542, 76 FR 50889, Aug. 17, 2011]

§ 1.249-1 Limitation on deduction of bond premium on repurchase.

(a) *Limitation—(1) General rule.* No deduction is allowed to the issuing corporation for any “repurchase premium” paid or incurred to repurchase a convertible obligation to the extent the repurchase premium exceeds a “normal call premium.”

(2) *Exception.* Under paragraph (e) of this section, the preceding sentence shall not apply to the extent the corporation demonstrates that such excess is attributable to the cost of borrowing and not to the conversion feature.

(b) *Obligations—(1) Definition.* For purposes of this section, the term *obligation* means any bond, debenture,

note, or certificate or other evidence of indebtedness.

(2) *Convertible obligation.* Section 249 applies to an obligation which is convertible into the stock of the issuing corporation or a corporation which, at the time the obligation is issued or repurchased, is in control of or controlled by the issuing corporation. For purposes of this subparagraph, the term *control* has the meaning assigned to such term by section 368(c).

(3) *Comparable nonconvertible obligation.* A nonconvertible obligation is comparable to a convertible obligation if both obligations are of the same grade and classification, with the same issue and maturity dates, and bearing the same rate of interest. The term *comparable nonconvertible obligation* does not include any obligation which is convertible into property.

(c) *Repurchase premium.* For purposes of this section, the term *repurchase premium* means the excess of the repurchase price paid or incurred to repurchase the obligation over its adjusted issue price (within the meaning of § 1.1275-1(b)) as of the repurchase date. For the general rules applicable to the deductibility of repurchase premium, see § 1.163-7(c). This paragraph (c) applies to convertible obligations repurchased on or after March 2, 1998.

(d) *Normal call premium—(1) In general.* Except as provided in subparagraph (2) of this paragraph, for purposes of this section, a *normal call premium* on a convertible obligation is an amount equal to a normal call premium on a nonconvertible obligation which is comparable to the convertible obligation. A normal call premium on a comparable nonconvertible obligation is a call premium specified in dollars under the terms of such obligation. Thus, if such a specified call premium is constant over the entire term of the obligation, the normal call premium is the amount specified. If, however, the specified call premium varies during the period the comparable nonconvertible obligation is callable or if such obligation is not callable over its entire term, the normal call premium is the amount specified for the period during the term of such comparable nonconvertible obligation which corresponds to the period

during which the convertible obligation was repurchased.

(2) *One-year's interest rule.* For a convertible obligation repurchased on or after March 2, 1998, a call premium specified in dollars under the terms of the obligation is considered to be a normal call premium on a nonconvertible obligation if the call premium applicable when the obligation is repurchased does not exceed an amount equal to the interest (including original issue discount) that otherwise would be deductible for the taxable year of repurchase (determined as if the obligation were not repurchased). The provisions of this subparagraph shall not apply if the amount of interest payable for the corporation's taxable year is subject under the terms of the obligation to any contingency other than repurchase prior to the close of such taxable year.

(e) *Exception—(1) In general.* If a repurchase premium exceeds a normal call premium, the general rule of paragraph (a) (1) of this section does not apply to the extent that the corporation demonstrates to the satisfaction of the Commissioner or his delegate that such repurchase premium is attributable to the cost of borrowing and is not attributable to the conversion feature. For purposes of this paragraph, if a normal call premium cannot be established under paragraph (d) of this section, the amount thereof shall be considered to be zero.

(2) *Determination of the portion of a repurchase premium attributable to the cost of borrowing and not attributable to the conversion feature.* (i) For purposes of subparagraph (1) of this paragraph, the portion of a repurchase premium which is attributable to the cost of borrowing and which is not attributable to the conversion feature is the amount by which the selling price of the convertible obligation increased between the dates it was issued and repurchased by reason of a decline in yields on comparable nonconvertible obligations traded on an established securities market or, if such comparable traded obligations do not exist, by reason of a decline in yields generally on nonconvertible obligations which are as nearly comparable as possible.

§ 1.249-1T

26 CFR Ch. I (4-1-13 Edition)

(ii) [Reserved] For further guidance, see § 1.249-1T(e)(2)(ii).

(iii) The relationship between selling price and yields in subdivision (i) of this subparagraph shall ordinarily be determined by means of standard bond tables.

(f) *Effective/applicability dates*—(1) *In general.* Under section 414(c) of the Tax Reform Act of 1969, the provisions of section 249 and this section shall apply to any repurchase of a convertible obligation occurring after April 22, 1969, other than a convertible obligation repurchased pursuant to a binding obligation incurred on or before April 22, 1969, to repurchase such convertible obligation at a specified call premium. A binding obligation on or before such date may arise if, for example, the issuer irrevocably obligates itself, on or before such date, to repurchase the convertible obligation at a specified price after such date, or if, for example, the issuer, without regard to the terms of the convertible obligation, negotiates a contract which, on or before such date, irrevocably obligates the issuer to repurchase the convertible obligation at a specified price after such date. A binding obligation on or before such date does not include a privilege in the convertible obligation permitting the issuer to call such convertible obligation after such date, which privilege was not exercised on or before such date.

(2) *Effect on transactions not subject to this section.* No inferences shall be drawn from the provisions of section 249 and this section as to the proper treatment of transactions not subject to such provisions because of the effective date limitations thereof. For provisions relating to repurchases of convertible bonds or other evidences of indebtedness to which section 249 and this section do not apply, see §§ 1.163-3(c) and 1.163-4(c).

(3) [Reserved] For further guidance, see § 1.249-1T(f)(3).

(g) *Example.* The provisions of this section may be illustrated by the following example:

Example. On May 15, 1968, corporation A issues a callable 20-year convertible bond at face for \$1,000 bearing interest at 10 percent per annum. The bond is convertible at any time into 2 shares of the common stock of

corporation A. Under the terms of the bond, the applicable call price prior to May 15, 1975, is \$1,100. On June 1, 1974, corporation A calls the bond for \$1,100. Since the repurchase premium, \$100 (i.e., \$1,100 minus \$1,000), was specified in dollars in the obligation and does not exceed 1 year's interest at the rate fixed in the obligation, the \$100 is considered under paragraph (d) (2) of this section to be a normal call premium on a comparable nonconvertible obligation. Accordingly, A may deduct the \$100 under § 1.163-3(c).

[T.D. 7259, 38 FR 4254, Feb. 12, 1973, as amended by T.D. 8746, 62 FR 68182, Dec. 31, 1997; T.D. 9533, 76 FR 39281, July 6, 2011]

§ 1.249-1T Limitation on deduction of bond premium on repurchase (temporary).

(a) through (e)(2)(i) [Reserved] For further guidance, see § 1.249-1(a) through (e)(2)(i).

(ii) In determining the amount under § 1.249-1(e)(2)(i), appropriate consideration shall be given to all factors affecting the selling price or yields of comparable nonconvertible obligations. Such factors include general changes in prevailing yields of comparable obligations between the dates the convertible obligation was issued and repurchased and the amount (if any) by which the selling price of the nonconvertible obligation was affected by reason of any change in the issuing corporation's credit quality or the credit quality of the obligation during such period (determined on the basis of widely published financial information or on the basis of other relevant facts and circumstances which reflect the relative credit quality of the corporation or the comparable obligation).

(e)(2)(iii) through (f)(2) [Reserved] For further guidance, see § 1.249-1(e)(2)(iii) through (f)(2).

(3) *Portion of repurchase premium attributable to cost of borrowing.* Paragraph (e)(2)(ii) of this section applies to any repurchase of a convertible obligation occurring on or after July 6, 2011.

(g) [Reserved] For further guidance, see § 1.249-1(g).

(h) *Expiration date.* The applicability of this section expires on or before July 1, 2014.

[T.D. 9533, 76 FR 39281, July 6, 2011]