

issued before October 1, 1942. Whether the money used to retire the bonds can be traced back and identified as the money paid in for the stock will have evidentiary value, but will not be conclusive, in determining whether the stock was issued to refund or replace the bonds. Similarly, whether the amount of money used to retire the bonds was smaller than, equal to, or greater than that paid in for the stock, or whether the entire issue of bonds is retired, will be important, but not decisive, in making such determination.

(6) Preferred stock issued on or after October 1, 1942, by a corporation to refund or replace bonds or debentures of a second corporation which were issued before October 1, 1942, or to refund or replace other preferred stock of such second corporation, may be considered as having been issued before October 1, 1942, if such new stock was issued (i) in a transaction which is a reorganization within the meaning of section 368(a) or the corresponding provisions of the Internal Revenue Code of 1939; or (ii) in a transaction to which section 371 (relating to insolvency reorganizations), or the corresponding provisions of the Internal Revenue Code of 1939, is applicable; or (iii) in a transaction which is subject to the provisions of Part VI, Subchapter O, Chapter 1 of the Code (relating to exchanges and distributions in obedience to orders of the Securities and Exchange Commission) or to the corresponding provisions of the Internal Revenue Code of 1939. Whether the stock actually was issued to refund or replace bonds or debentures of the second corporation issued before October 1, 1942, or to refund or replace preferred stock of such second corporation, shall be determined under the same principles as if only one corporation were involved. A corporation may issue stock to refund or replace its own bonds, debentures, or other preferred stock in a transaction which is a reorganization within the meaning of section 368(a) or the corresponding provisions of the Internal Revenue Code of 1939, in a transaction to which section 371 or the corresponding provisions of the Internal Revenue Code of 1939 is applicable, or in a transaction which is subject to the provisions of Part VI, Subchapter O, Chapter 1 of the Code, or

to the corresponding provisions of the Internal Revenue Code of 1939. The provisions of this paragraph, in addition, are applicable in case a corporation issues stock on or after October 1, 1942, to refund or replace its own bonds, debentures, or other preferred stock even though the issuance of such stock may not fall within one of the categories enumerated above.

(7) Even though stock issued on or after October 1, 1942, is considered as having been issued before October 1, 1942, by reason of having been issued to refund or replace bonds or debentures issued before October 1, 1942, or to refund or replace other preferred stock, such stock will not be deemed to be preferred stock within the meaning of section 247(b)(2), and no deduction will be allowable in respect of dividends paid on such stock, unless the stock fulfills all the other requirements of a preferred stock set forth in section 247(b)(2) and in this paragraph.

§ 1.248-1 Election to amortize organizational expenditures.

(a) *In general.* Under section 248(a), a corporation may elect to amortize organizational expenditures as defined in section 248(b) and § 1.248-1(b). In the taxable year in which a corporation begins business, an electing corporation may deduct an amount equal to the lesser of the amount of the organizational expenditures of the corporation, or \$5,000 (reduced (but not below zero) by the amount by which the organizational expenditures exceed \$50,000). The remainder of the organizational expenditures is deducted ratably over the 180-month period beginning with the month in which the corporation begins business. All organizational expenditures of the corporation are considered in determining whether the organizational expenditures exceed \$50,000, including expenditures incurred on or before October 22, 2004.

(b) *Organizational expenditures defined.* (1) Section 248(b) defines the term *organizational expenditures*. Such expenditures, for purposes of section 248 and this section, are those expenditures which are directly incident to the

creation of the corporation. An expenditure, in order to qualify as an organizational expenditure, must be (i) incident to the creation of the corporation, (ii) chargeable to the capital account of the corporation, and (iii) of a character which, if expended incident to the creation of a corporation having a limited life, would be amortizable over such life. An expenditure which fails to meet each of these three tests may not be considered an organizational expenditure for purposes of section 248 and this section.

(2) The following are examples of organizational expenditures within the meaning of section 248 and this section: legal services incident to the organization of the corporation, such as drafting the corporate charter, by-laws, minutes of organizational meetings, terms of original stock certificates, and the like; necessary accounting services; expenses of temporary directors and of organizational meetings of directors or stockholders; and fees paid to the State of incorporation.

(3) The following expenditures are not organizational expenditures within the meaning of section 248 and this section:

(i) Expenditures connected with issuing or selling shares of stock or other securities, such as commissions, professional fees, and printing costs. This is so even where the particular issue of stock to which the expenditures relate is for a fixed term of years;

(ii) Expenditures connected with the transfer of assets to a corporation.

(4) Expenditures connected with the reorganization of a corporation, unless directly incident to the creation of a corporation, are not organizational expenditures within the meaning of section 248 and this section.

(c) *Time and manner of making election.* A corporation is deemed to have made an election under section 248(a) to amortize organizational expenditures as defined in section 248(b) and § 1.248-1(b) for the taxable year in which the corporation begins business. A corporation may choose to forgo the deemed election by affirmatively electing to capitalize its organizational expenditures on a timely filed Federal income tax return (including extensions) for the taxable year in which the cor-

poration begins business. The election either to amortize organizational expenditures under section 248(a) or to capitalize organizational expenditures is irrevocable and applies to all organizational expenditures of the corporation. A change in the characterization of an item as an organizational expenditure is a change in method of accounting to which sections 446 and 481(a) apply if the corporation treated the item consistently for two or more taxable years. A change in the determination of the taxable year in which the corporation begins business also is treated as a change in method of accounting if the corporation amortized organizational expenditures for two or more taxable years.

(d) *Determination of when corporation begins business.* The deduction allowed under section 248 must be spread over a period beginning with the month in which the corporation begins business. The determination of the date the corporation begins business presents a question of fact which must be determined in each case in light of all the circumstances of the particular case. The words “begins business,” however, do not have the same meaning as “in existence.” Ordinarily, a corporation begins business when it starts the business operations for which it was organized; a corporation comes into existence on the date of its incorporation. Mere organizational activities, such as the obtaining of the corporate charter, are not alone sufficient to show the beginning of business. If the activities of the corporation have advanced to the extent necessary to establish the nature of its business operations, however, it will be deemed to have begun business. For example, the acquisition of operating assets which are necessary to the type of business contemplated may constitute the beginning of business.

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

Example 1. Expenditures of \$5,000 or less Corporation X, a calendar year taxpayer, incurs \$3,000 of organizational expenditures after October 22, 2004, and begins business on July 1, 2011. 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 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).

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§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,