

of reasonable compensation for services, are not deductible from gross income.

§ 1.162-10 Certain employee benefits.

(a) *In general.* Amounts paid or accrued by a taxpayer on account of injuries received by employees and lump sum amounts paid or accrued as compensation for injuries, are proper deductions as ordinary and necessary expenses. Such deductions are limited to the amount not compensated for by insurance or otherwise. Amounts paid or accrued within the taxable year for dismissal wages, unemployment benefits, guaranteed annual wages, vacations, or a sickness, accident, hospitalization, medical expense, recreational, welfare, or similar benefit plan, are deductible under section 162(a) if they are ordinary and necessary expenses of the trade or business. However, except as provided in paragraph (b) of this section, such amounts shall not be deductible under section 162(a) if, under any circumstances, they may be used to provide benefits under a stock bonus, pension, annuity, profit-sharing, or other deferred compensation plan of the type referred to in section 404(a). In such an event, the extent to which these amounts are deductible from gross income shall be governed by the provisions of section 404 and the regulations issued thereunder.

(b) *Certain negotiated plans.* (1) Subject to the limitations set forth in subparagraphs (2) and (3) of this paragraph, contributions paid by an employer under a plan under which such contributions are held in a welfare trust for the purpose of paying (either from principal or income or both) for the benefit of employees, their families, and dependents, at least medical or hospital care, and pensions on retirement or death of employees, are deductible when paid as business expenses under section 162(a).

(2) For the purpose of subparagraph (1) of this paragraph, the word "plan" means any plan established prior to January 1, 1954, as a result of an agreement between employee representatives and the Government of the United States, during a period of Government operation, under seizure powers, of a major part of the productive

facilities of the industry in which the employer claiming the deduction is engaged. The phrase "plan established prior to January 1, 1954, as a result of an agreement" is intended primarily to cover a trust established under the terms of such an agreement. It also includes a trust established under a plan of an employer, or group of employers, who, by reason of producing the same commodity, are in competition with the employers whose facilities were seized and who would therefore be expected to establish such a trust as a reasonable measure to maintain a sound position in the labor market producing the commodity. For example, if a trust was established under such an agreement in the bituminous coal industry, a similar trust established in the anthracite coal industry within a reasonable time, but before January 1, 1954, would qualify under subparagraph (1) of this paragraph.

(3) If any trust described in subparagraph (2) of this paragraph becomes qualified for exemption from tax under the provisions of section 501(a), the deductibility of contributions by an employer to such trust on or after any date of such qualification shall no longer be governed by the provisions of section 162, even though the trust may later lose its exemption from tax under section 501(a).

(c) *Other plans providing deferred compensation.* For rules relating to the deduction of amounts paid to or under a stock bonus, pension, annuity, or profit-sharing plan or amounts paid or accrued under any other plan deferring the receipt of compensation, see section 404 and the regulations thereunder.

§ 1.162-10T Questions and answers relating to the deduction of employee benefits under the Tax Reform Act of 1984; certain limits on amounts deductible (temporary).

Q-1: How does the amendment of section 404(b) by the Tax Reform Act of 1984 affect the deduction of employee benefits under section 162 of the Internal Revenue Code?

A-1: As amended by the Tax Reform Act of 1984, section 404(b) clarifies that section 404(a) and (d) (in the case of employees and nonemployees, respectively) shall govern the deduction of

contributions paid or compensation paid or incurred under a plan, or method or arrangement, deferring the receipt of compensation or providing for deferred benefits. Section 404(a) and (d) requires that such a contribution or compensation be paid or incurred for purposes of section 162 or 212 and satisfy the requirements for deductibility under either of these sections. However, notwithstanding the above, section 404 does not apply to contributions paid or accrued with respect to a "welfare benefit fund" (as defined in section 419(e)) after July 18, 1984, in taxable years of employers (and payors) ending after that date.

Also, section 463 shall govern the deduction of vacation pay by a taxpayer that has elected the application of such section. Section 404(b), as amended, generally applies to contributions paid and compensation paid or incurred after July 18, 1984, in taxable years of employers (and payors) ending after that date. See Q&A-3 of §1.404(b)-1T. For rules relating to the deduction of contributions attributable to the provision of deferred benefits, see section 404 (a), (b) and (d) and §1.404(a)-1T, §1.404(b)-1T and §1.404(d)-1T. For rules relating to the deduction of contributions paid or accrued with respect to a welfare benefit fund, see section 419, §1.419-1T and §1.419A-2T. For rules relating to the deduction of vacation pay for which an election is made under section 463, see §301.9100-16T of this chapter and §1.463-1T.

Q-2: How does the enactment of section 419 by the Tax Reform Act of 1984 affect the deduction of employee benefits under section 162?

A-2: As enacted by the Tax Reform Act of 1984, section 419 shall govern the deduction of contributions paid or accrued by an employer (or a person receiving services under section 419(g)) with respect to a "welfare benefit fund" (within the meaning of section 419(e)) after December 31, 1985, in taxable years of the employer (or person receiving the services) ending after that date. Section 419(a) requires that such a contribution be paid or accrued for purposes of section 162 or 212 and satisfy the requirements for deductibility under either of those sections. Generally, subject to a binding con-

tract exception (as described in section 511(e)(5) of the Tax Reform Act of 1984), section 419 shall also govern the deduction of the contribution of a facility (or other contribution used to acquire or improve a facility) to a welfare benefit fund after June 22, 1984. See Q&A-11 of §1.419-1T. In the case of a welfare benefit fund maintained pursuant to a collective bargaining agreement, section 419 applies to the extent provided under the special effective date rule described in Q&A-2 of §1.419-1T and the special rules of §1.419A-2T. For rules relating to the deduction of contributions paid or accrued with respect to a welfare benefit fund, see section 419 and §1.419-1T.

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§ 1.162-11 Rentals.

(a) *Acquisition of a leasehold.* If a leasehold is acquired for business purposes for a specified sum, the purchaser may take as a deduction in his return an aliquot part of such sum each year, based on the number of years the lease has to run. Taxes paid by a tenant to or for a landlord for business property are additional rent and constitute a deductible item to the tenant and taxable income to the landlord, the amount of the tax being deductible by the latter. For disallowance of deduction for income taxes paid by a lessee corporation pursuant to a lease arrangement with the lessor corporation, see section 110 and the regulations thereunder. See section 178 and the regulations thereunder for rules governing the effect to be given renewal options in amortizing the costs incurred after July 28, 1958 of acquiring a lease. See §1.197-2 for rules governing the amortization of costs to acquire limited interests in section 197 intangibles.

(b) *Improvements by lessee on lessor's property.* (1) The cost to a lessee of erecting buildings or making permanent improvements on property of which he is the lessee is a capital investment, and is not deductible as a business expense. If the estimated useful life in the hands of the taxpayer of the building erected or of the improvements made, determined without regard to the terms of the lease, is longer than the remaining period of the lease,