

deduction, see section 461. For provisions disallowing any deduction for the tax paid at the source on interest from tax-free covenant bonds, see section 1451(f).

[T.D. 6780, 29 FR 18145, Dec. 22, 1964, as amended by T.D. 7577, 43 FR 59357, Dec. 20, 1978]

**§ 1.164-2 Deduction denied in case of certain taxes.**

This section and § 1.275 describe certain taxes for which no deduction is allowed. In the case of taxable years beginning before January 1, 1964, the denial is provided for by section 164(b) (prior to being amended by section 207 of the Revenue Act of 1964 (78 Stat. 40)). In the case of taxable years beginning after December 31, 1963, the denial is governed by sections 164 and 275. No deduction is allowed for the following taxes:

(a) *Federal income taxes.* Federal income taxes, including the taxes imposed by section 3101, relating to the tax on employees under the Federal Insurance Contributions Act (chapter 21 of the Code); sections 3201 and 3211, relating to the taxes on railroad employees and railroad employee representatives; section 3402, relating to the tax withheld at source on wages; and by corresponding provisions of prior internal revenue laws.

(b) *Federal war profits and excess profits taxes.* Federal war profits and excess profits taxes including those imposed by Title II of the Revenue Act of 1917 (39 Stat. 1000), Title III of the Revenue Act of 1918 (40 Stat. 1088), Title III of the Revenue Act of 1921 (42 Stat. 271), section 216 of the National Industrial Recovery Act (48 Stat. 208), section 702 of the Revenue Act of 1934 (48 Stat. 770), Subchapter D, Chapter 1 of the Internal Revenue Code of 1939, and Subchapter E, Chapter 2 of the Internal Revenue Code of 1939.

(c) *Estate and gift taxes.* Estate, inheritance, legacy, succession, and gift taxes.

(d) *Foreign income, war profits, and excess profits taxes.* 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, relating to

the credit for taxes of foreign countries and possessions of the United States.

(e) *Real property taxes.* Taxes on real property, to the extent that section 164(d) and § 1.164-6 require such taxes to be treated as imposed on another taxpayer.

(f) *Federal duties and excise taxes.* Federal import or tariff duties, business, license, privilege, excise, and stamp taxes (not described in paragraphs (a), (b), (c), or (h) of this section, or § 1.164-4) paid or accrued within the taxable year. The fact that any such tax is not deductible as a tax under section 164 does not prevent (1) its deduction under section 162 or section 212, provided it represents an ordinary and necessary expense paid or incurred during the taxable year by a corporation or an individual in the conduct of any trade or business or, in the case of an individual for the production or collection of income, for the management, conservation, or maintenance of property held for the production of income, or in connection with the determination, collection, or refund of any tax, or (2) its being taken into account during the taxable year by a corporation or an individual as a part of the cost of acquiring or producing property in the trade or business or, in the case of an individual, as a part of the cost of property held for the production of income with respect to which it relates.

(g) *Taxes for local benefits.* Except as provided in § 1.164-4, taxes assessed against local benefits of a kind tending to increase the value of the property assessed.

(h) *Excise tax on real estate investment trusts.* The excise tax imposed on certain real estate investment trusts by section 4981.

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**§ 1.164-3 Definitions and special rules.**

For purposes of section 164 and § 1.164-1 to § 1.164-8, inclusive—

(a) *State or local taxes.* A State or local tax includes only a tax imposed by a State, a possession of the United States, or a political subdivision of any of the foregoing, or by the District of Columbia.

(b) *Real property taxes.* The term “real property taxes” means taxes imposed

on interests in real property and levied for the general public welfare, but it does not include taxes assessed against local benefits. See § 1.164-4.

(c) *Personal property taxes.* The term “personal property tax” means an ad valorem tax which is imposed on an annual basis in respect of personal property. To qualify as a personal property tax, a tax must meet the following three tests:

(1) The tax must be ad valorem—that is, substantially in proportion to the value of the personal property. A tax which is based on criteria other than value does not qualify as ad valorem. For example, a motor vehicle tax based on weight, model year, and horsepower, or any of these characteristics is not an ad valorem tax. However, a tax which is partly based on value and partly based on other criteria may qualify in part. For example, in the case of a motor vehicle tax of 1 percent of value plus 40 cents per hundred-weight, the part of the tax equal to 1 percent of value qualifies as an ad valorem tax and the balance does not qualify.

(2) The tax must be imposed on an annual basis, even if collected more frequently or less frequently.

(3) The tax must be imposed in respect of personal property. A tax may be considered to be imposed in respect of personal property even if in form it is imposed on the exercise of a privilege. Thus, for taxable years beginning after December 31, 1963, State and local taxes on the registration or licensing of highway motor vehicles are not deductible as personal property taxes unless and to the extent that the tests prescribed in this subparagraph are met. For example, an annual ad valorem tax qualifies as a personal property tax although it is denominated a registration fee imposed for the privilege of registering motor vehicles or of using them on the highways.

(d) *Foreign taxes.* The term “foreign tax” includes only a tax imposed by the authority of a foreign country. A tax imposed by a political subdivision of a foreign country is considered to be imposed by the authority of that foreign country.

(e) *Sales tax.* (1) The term “sales tax” means a tax imposed upon persons en-

gaged in selling tangible personal property, or upon the consumers of such property, including persons selling gasoline or other motor vehicle fuels at wholesale or retail, which is a stated sum per unit of property sold or which is measured by the gross sales price or the gross receipts from the sale. The term also includes a tax imposed upon persons engaged in furnishing services which is measured by the gross receipts for furnishing such services.

(2) In general, the term “consumer” means the ultimate user or purchaser; it does not include a purchaser such as a retailer, who acquires the property for resale.

(f) *General sales tax.* A “general sales tax” is a sales tax which is imposed at one rate in respect of the sale at retail of a broad range of classes of items. No foreign sales tax is deductible under section 164(a) and paragraph (a)(4) of § 1.164-1. To qualify as a general sales tax, a tax must meet the following two tests:

(1) The tax must be a tax in respect of sales at retail. This may include a tax imposed on persons engaged in selling property at retail or furnishing services at retail, for example, if the tax is measured by gross sales price or by gross receipts from sales or services. Rentals qualify as sales at retail if so treated under applicable State sales tax laws.

(2) The tax must be general—that is, it must be imposed at one rate in respect of the retail sales of a broad range of classes of items. A sales tax is considered to be general although imposed on sales of various classes of items at more than one rate provided that one rate applies to the retail sales of a broad range of classes of items. The term “items” includes both commodities and services.

(g) *Special rules relating to general sales taxes.* (1) A sales tax which is general is usually imposed at one rate in respect of the retail sales of all tangible personal property (with exceptions and additions). However, a sales tax which is selective—that is, a tax which applies at one rate with respect to retail sales of specified classes of items also qualifies as general if the specified classes represent a broad range of classes of items. A selective

sales tax which does not apply at one rate to the retail sales of a broad range of classes of items is not general. For example, a tax which applies only to sales of alcoholic beverages, tobacco, admissions, luxury items, and a few other items is not general. Similarly, a tax imposed solely on services is not general. However, a selective sales tax may be deemed to be part of the general sales tax and hence may be deductible, even if imposed by a separate title, etc., of the State or local law, if imposed at the same rate as the general rate of tax (as defined in subparagraph (4) of this paragraph) which qualifies a tax in the taxing jurisdiction as a general sales tax. For example, if a State has a 5 percent general sales tax and a separate selective sales tax of 5 percent on transient accommodations, the tax on transient accommodations is deductible.

(2) A tax is imposed at one rate only if it is imposed at that rate on generally the same base for all items subject to tax. For example, a sales tax imposed at a 3 percent rate on 100 percent of the sales price of some classes of items and at a 3 percent rate on 50 percent of the sales price of other classes of items would not be imposed at one rate with respect to all such classes. However, a tax is considered to be imposed at one rate although it allows dollar exemptions, if the exemptions are designed to exclude all sales under a certain dollar amount. For example, a tax may be imposed at one rate although it applies to all sales of tangible personal property but applies only to sales amounting to more than 10 cents.

(3) The fact that a sales tax exempts food, clothing, medical supplies, and motor vehicles, or any of them, shall not be taken into account in determining whether the tax applies to a broad range of classes of items. The fact that a sales tax applies to food, clothing, medical supplies, and motor vehicles, or any of them, at a rate which is lower than the general rate of tax (as defined in subparagraph (4) of this paragraph) is not taken into account in determining whether the tax is imposed at one rate on the retail sales of a broad range of classes of items. For purposes of this section, the

term "food" means food for human consumption off the premises where sold, and the term "medical supplies" includes drugs, medicines, and medical devices.

(4) Except in the case of a lower rate of tax applicable in respect of food, clothing, medical supplies, and motor vehicles, or any of them, no deduction is allowed for a general sales tax in respect of any item if the tax is imposed on such item at a rate other than the general rate of tax. The general rate of tax is the one rate which qualifies a tax in a taxing jurisdiction as a general sales tax because the tax is imposed at such one rate on a broad range of classes of items. There can be only one general rate of tax in any one taxing jurisdiction. However, a general sales tax imposed at a lower rate or rates on food, clothing, motor vehicles, and medical supplies, or any of them, may nonetheless be deductible with respect to such items. For example, a sales tax which is imposed at 1 percent with respect to food, imposed at 3 percent with respect to a broad range of classes of tangible personal property, and imposed at 4 percent with respect to transient accommodations would qualify as a general sales tax. Taxes paid at the 1 percent and the 3 percent rates are deductible, but tax paid at the 4 percent rate is not deductible. The fact that a sales tax provides for the adjustment of the general rate of tax to reflect the sales tax rate in another taxing jurisdiction shall not be taken into account in determining whether the tax is imposed at one rate on the retail sales of a broad range of classes of items. Moreover, a general sales tax imposed at a lower rate with respect to an item in order to reflect the tax rate in another jurisdiction is also deductible at such lower rate. For example, State E imposes a general sales tax whose general rate is 3 percent. The State E sales tax law provides that in areas bordering on States with general sales taxes, selective sales taxes, or special excise taxes, the rate applied in the adjoining State will be used if such rate is under 3 percent. State F imposes a 2 percent sales tax. The 2 percent sales tax paid by residents of State E in areas bordering on State F is deductible.

(h) *Compensating use taxes.* A compensating use tax in respect of any item is treated as a general sales tax. The term "compensating use tax" means, in respect of any item, a tax which is imposed on the use, storage, or consumption of such item and which is complementary to a general sales tax which is deductible with respect to sales of similar items.

(i) *Special rules relating to compensating use taxes.* (1) In general, a use tax on an item is complementary to a general sales tax on similar items if the use tax is imposed on an item which was not subject to such general sales tax but which would have been subject to such general sales tax if the sale of the item had taken place within the jurisdiction imposing the use tax. For example, a tax imposed by State A on the use of a motor vehicle purchased in State B is complementary to the general sales tax of State A on similar items, if the latter tax applies to motor vehicles sold in State A.

(2) Since a compensating use tax is treated as a general sales tax, it is subject to the rule of subparagraph (C) of section 164(b)(2) and paragraph (g)(4) of this section that no deduction is allowed for a general sales tax imposed in respect of an item at a rate other than the general rate of tax (except in the case of lower rates on the sale of food, clothing, medical supplies, and motor vehicles). The fact that a compensating use tax in respect of any item provides for an adjustment in the rate of the compensating use tax or the amount of such tax to be paid on account of a sales tax on such item imposed by another taxing jurisdiction is not taken into account in determining whether the compensating use tax is imposed in respect of the item at a rate other than the general rate of tax. For example, a compensating use tax imposed by State C on the use of an item purchased in State D is considered to be imposed at the general rate of tax even though the tax imposed by State C allows a credit for any sales tax paid on such item in State D, or the rate of such compensating use tax is adjusted to reflect the rate of sales tax imposed by State D.

[T.D. 6780, 29 FR 18146, Dec. 22, 1964]

#### § 1.164-4 Taxes for local benefits.

(a) So-called taxes for local benefits referred to in paragraph (g) of § 1.164-2, more properly assessments, paid for local benefits such as street, sidewalk, and other like improvements, imposed because of and measured by some benefit inuring directly to the property against which the assessment is levied are not deductible as taxes. A tax is considered assessed against local benefits when the property subject to the tax is limited to property benefited. Special assessments are not deductible, even though an incidental benefit may inure to the public welfare. The real property taxes deductible are those levied for the general public welfare by the proper taxing authorities at a like rate against all property in the territory over which such authorities have jurisdiction. Assessments under the statutes of California relating to irrigation, and of Iowa relating to drainage, and under certain statutes of Tennessee relating to levees, are limited to property benefited, and if the assessments are so limited, the amounts paid thereunder are not deductible as taxes. For treatment of assessments for local benefits as adjustments to the basis of property, see section 1016(a)(1) and the regulations thereunder.

(b)(1) Insofar as assessments against local benefits are made for the purpose of maintenance or repair or for the purpose of meeting interest charges with respect to such benefits, they are deductible. In such cases, the burden is on the taxpayer to show the allocation of the amounts assessed to the different purposes. If the allocation cannot be made, none of the amount so paid is deductible.

(2) Taxes levied by a special taxing district which was in existence on December 31, 1963, for the purpose of retiring indebtedness existing on such date, are deductible, to the extent levied for such purpose, if (i) the district covers the whole of at least one county, (ii) if at least 1,000 persons are subject to the taxes levied by the district, and (iii) if the district levies its assessments annually at a uniform rate on the same