Internal Revenue Service, Treasury

§ 5c.168(f)(8)–8

Loss of section 168(f)(8) protection; recapture.

(a) In general. Upon the occurrence of an event that causes an agreement to cease to be characterized as a lease under section 168(f)(8), the characterization of the lessor and lessee shall be determined without regard to section 168(f)(8).

(b) Events which cause an agreement to cease to be characterized as a lease. A disqualifying event shall cause an agreement to cease to be treated as a lease under section 168(f)(8) as of the date of the disqualifying event. A disqualifying event shall include the following:

(1) The lessor sells or assigns its interest in the lease or in the qualified leased property in a taxable transaction.

(2) The failure by the lessor to file a copy of the information return (or applicable statement) with its income tax return as required in §5c.168(f)(8)–2(a)(3)(i).

(3) The lessee (or any transferee of the lessee’s interest) sells or assigns its interest in the lease or in the qualified leased property to a third party in a taxable transaction described in section 168(f)(8)–2(a)(6) and the transferee fails to execute, within the prescribed time, the consent described in §5c.168(f)(8)–2(a)(5), or either the lessor or the transferee fail to file statements with their income tax returns as required by that paragraph.

(4) The property ceases to be section 38 property as defined in §1.168(f)(1)(ii) and §5c.168(f)(8)–4.

(7) The lease terminates.

(8) The property becomes subject to more than one lease for which an election is made under section 168(f)(8).

(9) Retirements and casualties. [Reserved]

(10) The property is transferred in a bankruptcy or similar proceeding and not all lenders with perfected and timely interests in the property specifically exclude or release the Federal income tax ownership of the property as required under §5c.168(f)(8)–2(a)(6)(iii).

(12) The property is transferred subsequent to a bankruptcy or similar proceeding and the lessor fails to furnish notice to the transferee prior to the transfer or fails to file a statement with its income tax return, and either the lessor fails to secure the transferee’s consent or the lessor or the transferee fail to file statements with their returns.
(13) The property is leased under the provisions of section 168(f)(8)(D)(ii) and §5c.168(f)(8)–6(b)(3) and ceases to be a qualified mass commuting vehicle.

(14) The failure by the lessor to file the required information return described in §5c.168(f)(8)–2 (a)(3)(ii) by January 31, 1982, unless the lessee files such return by January 31, 1982.

(c) Recapture. The required amount of recapture of the investment tax credit and of accelerated cost recovery deductions after a disqualifying event shall be determined under sections 47 and 1245, respectively.

(d) Consequences of loss of safe harbor protection. The tax consequences of a disqualifying event depend upon the characterization of the parties without regard to section 168(f)(8). If the lessee would be the owner of the property without regard to section 168(f)(8), the disqualifying event will be deemed to be a sale of the qualified leased property by the lessor to the lessee. The amount realized by the lessor on the sale will include the outstanding amount (if any) of the lessor’s debt on the property plus the sum of any other consideration received by the lessor. A disposition that results from a disqualifying event shall not be treated as an installment sale under section 453.

(e) Examples. The application of the provisions of this section may be illustrated by the following examples:

Example (1). M Corp. and N Corp. enter into a sale and leaseback transaction in which the leaseback agreement is characterized as a lease under section 168(f)(8) and M is treated as the lessee. In the second year of the lease, M becomes an electing small business corporation under subchapter S. The agreement ceases to be treated as a lease under section 168(f)(8) as of the date of the subchapter S election. Without respect to section 168(f)(8), N would be considered the owner of the property without regard to section 168(f)(8), upon the termination of the lease the property will be deemed to be sold by Q to P for the amount of the purchase money debt outstanding with respect to the property.

Example (2). Q Corp. (as lessor) and P Corp. (as lessee) enter into a lease that is characterized as a lease under section 168(f)(8). The lease has a 6-year term. P has no option to renew the lease or to purchase the property. At the end of 6 years, if P would be considered the owner of the property without regard to section 168(f)(8), upon the termination of the lease the property will be deemed to be sold by Q to P for the amount of the purchase money debt outstanding with respect to the property.

Example (3).

Step (1). Compute tax under section 1301 and the regulations thereunder on all taxable income, including gains or losses on regulated futures contracts subject to section 1256(a) and the regulations thereunder, using rates applicable to the taxpayer for the taxable year which includes June 23, 1981.

Step (2). Compute tax under section 1301 and the regulations thereunder on all taxable income, including gains or losses on regulated futures contracts subject to section 1256(a) and the regulations thereunder, using rates applicable to the taxpayer for taxable years beginning in 1982.