PLAN AMENDMENTS NOT REQUIRED UNTIL JANUARY 1, 1989

For provisions directing that if any amendments made by subtitle A or subtitle C of title XI [§§ 1101–1147 and 1171–1177] or title XVIII [§§ 1800–1899A] of Pub. L. 99–514 require an amendment to any plan, such plan amendment shall not be required to be made before the first plan year beginning on or after Jan. 1, 1989, see section 1140 of Pub. L. 99–514, as amended, set out as a note under section 401 of this title.

§ 263A. Capitalization and inclusion in inventory costs of certain expenses

(a) Nondeductibility of certain direct and indirect costs

(1) In general

In the case of any property to which this section applies, any costs described in paragraph (2)—

(A) in the case of property which is inventory in the hands of the taxpayer, shall be included in inventory costs, and

(B) in the case of any other property, shall be capitalized.

(2) Allocable costs

The costs described in this paragraph with respect to any property are—

(A) the direct costs of such property, and

(B) such property's proper share of those indirect costs (including taxes) part or all of which are allocable to such property.

Any cost which (but for this subsection) could not be taken into account in computing taxable income for any taxable year shall not be treated as a cost described in this paragraph.

(b) Property to which section applies

Except as otherwise provided in this section, this section shall apply to—

(1) Property produced by taxpayer

Real or tangible personal property produced by the taxpayer.

(2) Property acquired for resale

(A) In general

Real or personal property described in section 1221(a)(1) which is acquired by the taxpayer for resale.

(B) Exception for taxpayer with gross receipts of $10,000,000 or less

Subparagraph (A) shall not apply to any personal property acquired during any taxable year by the taxpayer for resale if the average annual gross receipts of the taxpayer (or any predecessor) for the 3-taxable year period ending with the taxable year preceding such taxable year do not exceed $10,000,000.

(C) Aggregation rules, etc.

For purposes of subparagraph (B), rules similar to the rules of paragraphs (2) and (3) of section 448(c) shall apply.

For purposes of paragraph (1), the term ''tangible personal property'' shall include a film, sound recording, video tape, book, or similar property.

(c) General exceptions

(1) Personal use property

This section shall not apply to any property produced by the taxpayer for use by the taxpayer other than in a trade or business or an activity conducted for profit.

(2) Research and experimental expenditures

This section shall not apply to any amount allowable as a deduction under section 174.

(3) Certain development and other costs of oil and gas wells or other mineral property

This section shall not apply to any cost allowable as a deduction under section 167(h), 179B, 263(c), 263(i), 291(b)(2), 616, or 617.

(4) Coordination with long-term contract rules

This section shall not apply to any property produced by the taxpayer pursuant to a long-term contract.

(5) Timber and certain ornamental trees

This section shall not apply to—

(A) trees raised, harvested, or grown by the taxpayer other than trees described in clause (ii) of subsection (e)(4)(B) (after application of the last sentence thereof), and

(B) any real property underlying such trees.

(6) Coordination with section 59(e)

Paragraphs (2) and (3) shall apply to any amount allowable as a deduction under section 59(e) for qualified expenditures described in subparagraphs (B), (C), (D), and (E) of paragraph (2) thereof.

(d) Exception for farming businesses

(1) Section not to apply to certain property

(A) In general

This section shall not apply to any of the following which is produced by the taxpayer in a farming business:

(i) Any animal.

(ii) Any plant which has a preproductive period of 2 years or less.

(B) Exception for taxpayers required to use accrual method

Subparagraph (A) shall not apply to any corporation, partnership, or tax shelter required to use an accrual method of accounting under section 447 or 448(a)(3).

(2) Treatment of certain plants lost by reason of casualty

(A) In general

If plants bearing an edible crop for human consumption were lost or damaged (while in the hands of the taxpayer) by reason of freezing temperatures, disease, drought, pests, or casualty, this section shall not apply to any costs of the taxpayer of replanting plants bearing the same type of crop (whether on the same parcel of land on which such lost or damaged plants were located or any other parcel of land of the same acreage in the United States).

(B) Special rule for person with minority interest who materially participates

Subparagraph (A) shall apply to amounts paid or incurred by a person (other than the taxpayer described in subparagraph (A)) if—

(i) the taxpayer described in subparagraph (A) has an equity interest of more

than 50 percent in the plants described in subparagraph (A) at all times during the taxable year in which such amounts were paid or incurred, and

(ii) such other person holds any part of the remaining equity interest and materially participates in the planting, maintenance, cultivation, or development of such the plants described in subparagraph (A) during the taxable year in which such amounts were paid or incurred.

The determination of whether an individual materially participates in any activity shall be made in a manner similar to the manner in which such determination is made under section 2032A(e)(6).

(3) Election to have this section not apply

(A) In general

If a taxpayer makes an election under this paragraph, this section shall not apply to any plant produced in any farming business carried on by such taxpayer.

(B) Certain persons not eligible

No election may be made under this paragraph by a corporation, partnership, or tax shelter, if such corporation, partnership, or tax shelter is required to use an accrual method of accounting under section 447 or 448(a)(3).

(C) Special rule for citrus and almond growers

An election under this paragraph shall not apply with respect to any item which is attributable to the planting, cultivation, maintenance, or development of any citrus or almond grove (or part thereof) and which is incurred before the close of the 4th taxable year beginning with the taxable year in which the trees were planted. For purposes of the preceding sentence, the portion of a citrus or almond grove planted in 1 taxable year shall be treated separately from the portion of such grove planted in another taxable year.

(D) Election

Unless the Secretary otherwise consents, an election under this paragraph may be made only for the taxpayer's 1st taxable year which begins after December 31, 1986, and during which the taxpayer engages in a farming business. Any such election, once made, may be revoked only with the consent of the Secretary.

(e) Definitions and special rules for purposes of subsection (d)

(1) Recapture of expensed amounts on disposition

(A) In general

In the case of any plant with respect to which amounts would have been capitalized under subsection (a) but for an election under subsection (d)(3)—

(i) such plant (if not otherwise section 1245 property) shall be treated as section 1245 property, and

(ii) for purposes of section 1245, the recapture amount shall be treated as a deduction allowed for depreciation with respect to such property.

(B) Recapture amount

For purposes of subparagraph (A), the term ''recapture amount'' means any amount allowable as a deduction to the taxpayer which, but for an election under subsection (d)(3), would have been capitalized with respect to the plant.

(2) Effects of election on depreciation

(A) In general

If the taxpayer (or any related person) makes an election under subsection (d)(3), the provisions of section 168(g)(2) (relating to alternative depreciation) shall apply to all property of the taxpayer used predominantly in the farming business and placed in service in any taxable year during which any such election is in effect.

(B) Related person

For purposes of subparagraph (A), the term ''related person'' means—

(i) the taxpayer and members of the taxpayer's family,

(ii) any corporation (including an S corporation) if 50 percent or more (in value) of the stock of such corporation is owned (directly or through the application of section 318) by the taxpayer or members of the taxpayer's family,

(iii) a corporation and any other corporation which is a member of the same controlled group described in section 1563(a)(1), and

(iv) any partnership if 50 percent or more (in value) of the interests in such partnership is owned directly or indirectly by the taxpayer or members of the taxpayer's family.

(C) Members of family

For purposes of this paragraph, the term ''family'' means the taxpayer, the spouse of the taxpayer, and any of their children who have not attained age 18 before the close of the taxable year.

(3) Preproductive period

(A) In general

For purposes of this section, the term ''preproductive period'' means—

(i) in the case of a plant which will have more than 1 crop or yield, the period before the 1st marketable crop or yield from such plant, or

(ii) in the case of any other plant, the period before such plant is reasonably expected to be disposed of.

For purposes of this subparagraph, use by the taxpayer in a farming business of any supply produced in such business shall be treated as a disposition.

(B) Rule for determining period

In the case of a plant grown in commercial quantities in the United States, the preproductive period for such plant if grown in the United States shall be based on the nationwide weighted average preproductive period for such plant.

(4) Farming business

For purposes of this section—

(A) In general

The term ''farming business'' means the trade or business of farming.

(B) Certain trades and businesses included

The term ''farming business'' shall include the trade or business of—

(i) operating a nursery or sod farm, or

(ii) the raising or harvesting of trees bearing fruit, nuts, or other crops, or ornamental trees.

For purposes of clause (ii), an evergreen tree which is more than 6 years old at the time severed from the roots shall not be treated as an ornamental tree.

(5) Certain inventory valuation methods permitted

The Secretary shall by regulations permit the taxpayer to use reasonable inventory valuation methods to compute the amount required to be capitalized under subsection (a) in the case of any plant.

(f) Special rules for allocation of interest to property produced by the taxpayer

(1) Interest capitalized only in certain cases

Subsection (a) shall only apply to interest costs which are—

(A) paid or incurred during the production period, and

(B) allocable to property which is described in subsection (b)(1) and which has—

(i) a long useful life,

(ii) an estimated production period exceeding 2 years, or

(iii) an estimated production period exceeding 1 year and a cost exceeding $1,000,000.

(2) Allocation rules

(A) In general

In determining the amount of interest required to be capitalized under subsection (a) with respect to any property—

(i) interest on any indebtedness directly attributable to production expenditures with respect to such property shall be assigned to such property, and

(ii) interest on any other indebtedness shall be assigned to such property to the extent that the taxpayer's interest costs could have been reduced if production expenditures (not attributable to indebtedness described in clause (i)) had not been incurred.

(B) Exception for qualified residence interest

Subparagraph (A) shall not apply to any qualified residence interest (within the meaning of section 163(h)).

(C) Special rule for flow-through entities

Except as provided in regulations, in the case of any flow-through entity, this paragraph shall be applied first at the entity level and then at the beneficiary level.

(3) Interest relating to property used to produce property

This subsection shall apply to any interest on indebtedness allocable (as determined under paragraph (2)) to property used to produce property to which this subsection applies to the extent such interest is allocable (as so determined) to the produced property.

(4) Definitions

For purposes of this subsection—

(A) Long useful life

Property has a long useful life if such property is—

(i) real property, or

(ii) property with a class life of 20 years or more (as determined under section 168).

(B) Production period

The term ''production period'' means, when used with respect to any property, the period—

(i) beginning on the date on which production of the property begins, and

(ii) ending on the date on which the property is ready to be placed in service or is ready to be held for sale.

(C) Production expenditures

The term ''production expenditures'' means the costs (whether or not incurred during the production period) required to be capitalized under subsection (a) with respect to the property.

(g) Production

For purposes of this section—

(1) In general

The term ''produce'' includes construct, build, install, manufacture, develop, or improve.

(2) Treatment of property produced under contract for the taxpayer

The taxpayer shall be treated as producing any property produced for the taxpayer under a contract with the taxpayer; except that only costs paid or incurred by the taxpayer (whether under such contract or otherwise) shall be taken into account in applying subsection (a) to the taxpayer.

(h) Exemption for free lance authors, photographers, and artists

(1) In general

Nothing in this section shall require the capitalization of any qualified creative expense.

(2) Qualified creative expense

For purposes of this subsection, the term ''qualified creative expense'' means any expense—

(A) which is paid or incurred by an individual in the trade or business of such individual (other than as an employee) of being a writer, photographer, or artist, and

(B) which, without regard to this section, would be allowable as a deduction for the taxable year.

Such term does not include any expense related to printing, photographic plates, motion picture films, video tapes, or similar items.

(3) Definitions

For purposes of this subsection—

(A) Writer

The term ''writer'' means any individual if the personal efforts of such individual create

(or may reasonably be expected to create) a literary manuscript, musical composition (including any accompanying words), or dance score.

(B) Photographer

The term ''photographer'' means any individual if the personal efforts of such individual create (or may reasonably be expected to create) a photograph or photographic negative or transparency.

(C) Artist

(i) In general

The term ''artist'' means any individual if the personal efforts of such individual create (or may reasonably be expected to create) a picture, painting, sculpture, statue, etching, drawing, cartoon, graphic design, or original print edition.

(ii) Criteria

In determining whether any expense is paid or incurred in the trade or business of being an artist, the following criteria shall be taken into account:

(I) The originality and uniqueness of the item created (or to be created).

(II) The predominance of aesthetic value over utilitarian value of the item created (or to be created).

(D) Treatment of certain corporations

(i) In general

If—

(I) substantially all of the stock of a corporation is owned by a qualified employee-owner and members of his family (as defined in section 267(c)(4)), and

(II) the principal activity of such corporation is performance of personal services directly related to the activities of the qualified employee-owner and such services are substantially performed by the qualified employee-owner,

this subsection shall apply to any expense of such corporation which directly relates to the activities of such employee-owner in the same manner as if such expense were incurred by such employee-owner.

(ii) Qualified employee-owner

For purposes of this subparagraph, the term ''qualified employee-owner'' means any individual who is an employee-owner of the corporation (as defined in section 269A(b)(2)) and who is a writer, photographer, or artist.

(i) Regulations

The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including—

(1) regulations to prevent the use of related parties, pass-thru entities, or intermediaries to avoid the application of this section, and

(2) regulations providing for simplified procedures for the application of this section in the case of property described in subsection (b)(2).

(Added Pub. L. 99–514, title VIII, § 803(a), Oct. 22, 1986, 100 Stat. 2350; amended Pub. L. 100–647, title I, § 1008(b)(1)–(4), title VI, § 6026(a)–(c), Nov. 10, 1988, 102 Stat. 3437, 3438, 3691–3693; Pub. L. 101–239, title VII, § 7816(d)(1), Dec. 19, 1989, 103 Stat. 2420; Pub. L. 106–170, title V, § 532(c)(2)(B), Dec. 17, 1999, 113 Stat. 1930; Pub. L. 108–357, title III, § 338(b)(2), Oct. 22, 2004, 118 Stat. 1481; Pub. L. 109–58, title XIII, § 1329(b), Aug. 8, 2005, 119 Stat. 1020).

AMENDMENTS

2005—Subsec. (c)(3). Pub. L. 109–58 inserted ''167(h),'' after ''under section''.

2004—Subsec. (c)(3). Pub. L. 108–357, which directed amendment of par. (3) by inserting ''179B,'' after ''section'', was executed by making the insertion after ''section'' the second place it appeared to reflect the probable intent of Congress.

1999—Subsec. (b)(2)(A). Pub. L. 106–170 substituted ''1221(a)(1)'' for ''1221(1)''.

1989—Subsec. (h)(3)(D). Pub. L. 101–239 substituted ''corporations'' for ''personal service corporations'' in heading and amended text generally. Prior to amendment, text read as follows:

''(i) IN GENERAL.—In the case of a personal service corporation, this subsection shall apply to any expense of such corporation which directly relates to the activities of the qualified employee-owner in the same manner as if such expense were incurred by such employee-owner.

''(ii) QUALIFIED EMPLOYEE-OWNER.—The term 'qualified employee-owner' means any individual who is an employee-owner of the personal service corporation and who is a writer, photographer, or artist, but only if substantially all of the stock of such corporation is owned by such individual and members of his family (as defined in section 267(c)(4)).

''(iii) PERSONAL SERVICE CORPORATION.—For purposes of this subparagraph, the term 'personal service corporation' means any personal service corporation (as defined in section 269A(b)).''

1988—Subsec. (a)(2). Pub. L. 100–647, § 1008(b)(1), inserted at end ''Any cost which (but for this subsection) could not be taken into account in computing taxable income for any taxable year shall not be treated as a cost described in this paragraph.''

Subsec. (c)(3). Pub. L. 100–647, § 1008(b)(2)(A), substituted ''section 263(c), 263(i), 291(b)(2), 616, or 617'' for ''section 263(c), 616(a), or 617(a)''.

Subsec. (c)(6). Pub. L. 100–647, § 1008(b)(2)(B), added par. (6).

Subsec. (d)(1). Pub. L. 100–647, § 6026(b)(2)(A), substituted ''Section not to apply to certain property'' for ''Section to apply only if preproductive period is more than 2 years'' in heading.

Subsec. (d)(1)(A). Pub. L. 100–647, § 6026(b)(1), amended subpar. (A) generally. Prior to amendment, subpar. (A) read as follows: ''This section shall not apply to any plant or animal which is produced by the taxpayer in a farming business and which has a preproductive period of 2 years or less.''

Subsec. (d)(2)(B)(i). Pub. L. 100–647, § 1008(b)(3)(A), substituted ''the plants described in subparagraph (A) at all times during the taxable year in which such amounts were paid or incurred'' for ''such grove, orchard, or vineyard''.

Subsec. (d)(2)(B)(ii). Pub. L. 100–647, § 1008(b)(3)(B), substituted ''the plants described in subparagraph (A) during the taxable year in which such amounts were paid or incurred'' for ''such grove, orchard, or vineyard during the 4-taxable year period beginning with the taxable year in which the grove, orchard, or vineyard was lost or damaged''.

Subsec. (d)(3)(A). Pub. L. 100–647, § 6026(b)(2)(B), struck out ''or animal'' after ''plant''.

Subsec. (d)(3)(B). Pub. L. 100–647, § 6026(c), amended subpar. (B) generally. Prior to amendment, subpar. (B) read as follows: ''No election may be made under this paragraph—

''(i) by a corporation, partnership, or tax shelter, if such corporation, partnership, or tax shelter is re-

quired to use an accrual method of accounting under section 447 or 448(a)(3), or

''(ii) with respect to the planting, cultivation, maintenance, or development of pistachio trees.''

Subsec. (e). Pub. L. 100–647, §6026(b)(2)(B), struck out ''or animal'' after ''plant'' wherever appearing in pars. (1), (3), and (5).

Subsec. (f)(3). Pub. L. 100–647, §1008(b)(4), substituted ''allocable (as determined under paragraph (2)) to'' for ''incurred or continued in connection with'' and inserted ''(as so determined)'' after ''allocable''.

Subsecs. (h), (i). Pub. L. 100–647, §6026(a), added subsec. (h) and redesignated former subsec. (h) as (i).

EFFECTIVE DATE OF 2005 AMENDMENT

Amendment by Pub. L. 109–58 applicable to amounts paid or incurred in taxable years beginning after Aug. 8, 2005, see section 1329(c) of Pub. L. 109–58, set out as a note under section 167 of this title.

EFFECTIVE DATE OF 2004 AMENDMENT

Amendment by Pub. L. 108–357 applicable to expenses paid or incurred after Dec. 31, 2002, in taxable years ending after such date, see section 338(c) of Pub. L. 108–357, set out as an Effective Date note under section 179B of this title.

EFFECTIVE DATE OF 1999 AMENDMENT

Amendment by Pub. L. 106–170 applicable to any instrument held, acquired, or entered into, any transaction entered into, and supplies held or acquired on or after Dec. 17, 1999, see section 532(d) of Pub. L. 106–170, set out as a note under section 170 of this title.

EFFECTIVE DATE OF 1989 AMENDMENT

Amendment by Pub. L. 101–239 effective, except as otherwise provided, as if included in the provision of the Technical and Miscellaneous Revenue Act of 1988, Pub. L. 100–647, to which such amendment relates, see section 7817 of Pub. L. 101–239, set out as a note under section 1 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Amendment by section 1008(b)(1)–(4) of Pub. L. 100–647 effective, except as otherwise provided, as if included in the provision of the Tax Reform Act of 1986, Pub. L. 99–514, to which such amendment relates, see section 1019(a) of Pub. L. 100–647, set out as a note under section 1 of this title.

Section 6026(d) of Pub. L. 100–647, as amended by Pub. L. 101–239, title VII, §7816(d)(2), Dec. 19, 1989, 103 Stat. 2421, provided that:

''(1) IN GENERAL.—Except as otherwise provided in this paragraph, the amendments made by this section [amending this section] shall take effect as if included in the amendments made by section 803 of the Tax Reform Act of 1986 [section 803 of Pub. L. 99–514].

''(2) SUBSECTION (b).—

''(A) IN GENERAL.—The amendments made by subsection (b) [amending this section] shall apply to costs incurred after December 31, 1988, in taxable years ending after such date.

''(B) REVOCATION OF ELECTION.—If a taxpayer engaged in a farming business involving the production of animals having a preproductive period of more than 2 years made an election under section 263A(d)(3) of the 1986 Code for a taxable year beginning before January 1, 1989, such taxpayer may, without the consent of the Secretary of the Treasury or his delegate, revoke such election effective for the taxpayer's 1st taxable year beginning after December 31, 1988.''

EFFECTIVE DATE

Section 7831(d)(2) of Pub. L. 101–239 provided that: ''If any interest costs incurred after December 31, 1986, are attributable to costs incurred before January 1, 1987, the amendments made by section 803 of the Tax Reform Act of 1986 [section 803 of Pub. L. 99–514, enacting this section, amending sections 48, 267, 312, 447, 464, and 471 of this title, and repealing sections 189, 278, and 280 of this title] shall apply to such interest costs only to the extent such interest costs are attributable to costs which were required to be capitalized under section 263 of the Internal Revenue Code of 1954 and which would have been taken into account in applying section 189 of the Internal Revenue Code of 1954 (as in effect before its repeal by section 803 of the Tax Reform Act of 1986) or, if applicable, section 266 of such Code.''

Section 803(d) of Pub. L. 99–514, as amended by Pub. L. 100–647, title I, §1008(b)(7), Nov. 10, 1988, 102 Stat. 3438; Pub. L. 101–239, title VII, §7831(d)(1), Dec. 19, 1989, 103 Stat. 2426, provided that:

''(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [enacting this section, amending sections 48, 267, 312, 447, 464, and 471 of this title, and repealing sections 189, 278, and 280 of this title] shall apply to costs incurred after December 31, 1986, in taxable years ending after such date.

''(2) SPECIAL RULE FOR INVENTORY PROPERTY.—In the case of any property which is inventory in the hands of the taxpayer—

''(A) IN GENERAL.—The amendments made by this section shall apply to taxable years beginning after December 31, 1986.

''(B) CHANGE IN METHOD OF ACCOUNTING.—If the taxpayer is required by the amendments made by this section to change its method of accounting with respect to such property for any taxable year—

''(i) such change shall be treated as initiated by the taxpayer,

''(ii) such change shall be treated as made with the consent of the Secretary, and

''(iii) the period for taking into account the adjustments under section 481 by reason of such change shall not exceed 4 years.

''(3) SPECIAL RULE FOR SELF-CONSTRUCTED PROPERTY.—The amendments made by this section shall not apply to any property which is produced by the taxpayer for use by the taxpayer if substantial construction had occurred before March 1, 1986.

''(4) TRANSITIONAL RULE FOR CAPITALIZATION OF INTEREST AND TAXES.—

''(A) TRANSITION PROPERTY EXEMPTED FROM INTEREST CAPITALIZATION.—Section 263A of the Internal Revenue Code of 1986 (as added by this section) and the amendment made by subsection (b)(1) [repealing section 189 of this title] shall not apply to interest costs which are allocable to any property—

''(i) to which the amendments made by section 201 [amending sections 46, 167, 168, 178, 179, 280F, 291, 312, 465, 467, 514, 751, 1245, 4162, 6111, and 7701 of this title] do not apply by reason of sections 204(a)(1)(D) and (E) and 204(a)(5)(A) [set out as a note under section 168 of this title], and

''(ii) to which the amendments made by section 251 [amending sections 46 and 48 of this title and enacting provisions set out as a note under section 46 of this title] do not apply by reason of section 251(d)(3)(M) [set out as a note under section 46 of this title].

''(B) INTEREST AND TAXES.—Section 263A of such Code shall not apply to property described in the matter following subparagraph (B) of section 207(e)(2) of the Tax Equity and Fiscal Responsibility Act of 1982 [section 207(e)(2)(B) of Pub. L. 97–248, formerly set out as a note under section 189 of this title] to the extent it would require the capitalization of interest and taxes paid or incurred in connection with such property which are not required to be capitalized under section 189 of such Code (as in effect before the amendment made by subsection (b)(1)) [repealing section 189 of this title].

''(5) TRANSITION RULE CONCERNING CAPITALIZATION OF INVENTORY RULES.—In the case of a corporation which on the date of the enactment of this Act [Oct. 22, 1986] was a member of an affiliated group of corporations (within the meaning of section 1504(a) of the Internal Revenue Code of 1986), the parent of which—

''(A) was incorporated in California on April 15, 1925,

''(B) adopted LIFO accounting as of the close of the taxable year ended December 31, 1950, and

''(C) was, on May 22, 1986, merged into a Delaware corporation incorporated on March 12, 1986,

the amendments made by this section shall apply under a cut-off method whereby the uniform capitalization rules are applied only in costing layers of inventory acquired during taxable years beginning on or after January 1, 1987.

''(6) TREATMENT OF CERTAIN REHABILITATION PROJECT.—The amendments made by this section shall not apply to interest and taxes paid or incurred with respect to the rehabilitation and conversion of a certified historic building which was formerly a factory into an apartment project with 155 units, 39 units of which are for low-income families, if the project was approved for annual interest assistance on June 10, 1986, by the housing authority of the State in which the project is located.

''(7) SPECIAL RULE FOR CASUALTY LOSSES.—Section 263A(d)(2) of the Internal Revenue Code of 1986 (as added by this section) shall apply to expenses incurred on or after the date of the enactment of this Act [Oct. 22, 1986].''

ALLOCATION RATIO FOR APPORTIONING STORAGE COSTS AND RELATED HANDLING COSTS

Section 1008(b)(8) of Pub. L. 100–647 provided that: ''The allocation used in the regulations prescribed under section 263A(h)(2) of the Internal Revenue Code of 1986 for apportioning storage costs and related handling costs shall be determined by dividing the amount of such costs by the beginning inventory balances and the purchases during the year and by multiplying the resulting allocation ratio by inventory amounts determined in accordance with the provisions of the joint explanatory statement of the committee of conference of the conference report accompanying H.R. 3838 (H.R. Rept. No. 99–841, Vol. II., 99th Cong., 2d Sess. II–306–307 (1986)).''

AMORTIZATION OF PAST SERVICE PENSION COSTS

Pub. L. 100–203, title X, § 10204, Dec. 22, 1987, 101 Stat. 1330–394, provided that:

''(a) IN GENERAL.—For purposes of sections 263A and 460 of the Internal Revenue Code of 1986, the allocable costs (within the meaning of section 263A(a)(2) or section 460(c) of such Code, whichever is applicable) with respect to any property shall include contributions paid to or under a pension or annuity plan whether or not such contributions represent past service costs.

''(b) EFFECTIVE DATE.—

''(1) IN GENERAL.—Except as provided in paragraph (2), subsection (a) shall apply to costs incurred after December 31, 1987, in taxable years ending after such date.

''(2) SPECIAL RULE FOR INVENTORY PROPERTY.—In the case of any property which is inventory in the hands of the taxpayer—

''(A) IN GENERAL.—Subsection (a) shall apply to taxable years beginning after December 31, 1987.

''(B) CHANGE IN METHOD OF ACCOUNTING.—If the taxpayer is required by this section to change its method of accounting for any taxable year—

''(i) such change shall be treated as initiated by the taxpayer,

''(ii) such change shall be treated as made with the consent of the Secretary of the Treasury or his delegate, and

''(iii) the net amount of adjustments required by section 481 of the Internal Revenue Code of 1986 shall be taken into account over a period not longer than 4 taxable years.''

§ 264. Certain amounts paid in connection with insurance contracts

(a) General rule

No deduction shall be allowed for—

(1) Premiums on any life insurance policy, or endowment or annuity contract, if the taxpayer is directly or indirectly a beneficiary under the policy or contract.

(2) Any amount paid or accrued on indebtedness incurred or continued to purchase or carry a single premium life insurance, endowment, or annuity contract.

(3) Except as provided in subsection (d), any amount paid or accrued on indebtedness incurred or continued to purchase or carry a life insurance, endowment, or annuity contract (other than a single premium contract or a contract treated as a single premium contract) pursuant to a plan of purchase which contemplates the systematic direct or indirect borrowing of part or all of the increases in the cash value of such contract (either from the insurer or otherwise).

(4) Except as provided in subsection (e), any interest paid or accrued on any indebtedness with respect to 1 or more life insurance policies owned by the taxpayer covering the life of any individual, or any endowment or annuity contracts owned by the taxpayer covering any individual.

Paragraph (2) shall apply in respect of annuity contracts only as to contracts purchased after March 1, 1954. Paragraph (3) shall apply only in respect of contracts purchased after August 6, 1963. Paragraph (4) shall apply with respect to contracts purchased after June 20, 1986.

(b) Exceptions to subsection (a)(1)

Subsection (a)(1) shall not apply to—

(1) any annuity contract described in section 72(s)(5), and

(2) any annuity contract to which section 72(u) applies.

(c) Contracts treated as single premium contracts

For purposes of subsection (a)(2), a contract shall be treated as a single premium contract—

(1) if substantially all the premiums on the contract are paid within a period of 4 years from the date on which the contract is purchased, or

(2) if an amount is deposited after March 1, 1954, with the insurer for payment of a substantial number of future premiums on the contract.

(d) Exceptions

Subsection (a)(3) shall not apply to any amount paid or accrued by a person during a taxable year on indebtedness incurred or continued as part of a plan referred to in subsection (a)(3)—

(1) if no part of 4 of the annual premiums due during the 7-year period (beginning with the date the first premium on the contract to which such plan relates was paid) is paid under such plan by means of indebtedness,

(2) if the total of the amounts paid or accrued by such person during such taxable year for which (without regard to this paragraph) no deduction would be allowable by reason of subsection (a)(3) does not exceed $100.

(3) if such amount was paid or accrued on indebtedness incurred because of an unforeseen substantial loss of income or unforeseen sub-