

tributable to such policy or contract immediately before the insurance company's taxable year in which such event occurs, and

“(B) there shall be allowed as a deduction to such company for such taxable year under chapter 1 of such Code an amount equal to such unamortized balance.”

§ 265. Expenses and interest relating to tax-exempt income

(a) General rule

No deduction shall be allowed for—

(1) Expenses

Any amount otherwise allowable as a deduction which is allocable to one or more classes of income other than interest (whether or not any amount of income of that class or classes is received or accrued) wholly exempt from the taxes imposed by this subtitle, or any amount otherwise allowable under section 212 (relating to expenses for production of income) which is allocable to interest (whether or not any amount of such interest is received or accrued) wholly exempt from the taxes imposed by this subtitle.

(2) Interest

Interest on indebtedness incurred or continued to purchase or carry obligations the interest on which is wholly exempt from the taxes imposed by this subtitle.

(3) Certain regulated investment companies

In the case of a regulated investment company which distributes during the taxable year an exempt-interest dividend (including exempt-interest dividends paid after the close of the taxable year as described in section 855), that portion of any amount otherwise allowable as a deduction which the amount of the income of such company wholly exempt from taxes under this subtitle bears to the total of such exempt income and its gross income (excluding from gross income, for this purpose, capital gain net income, as defined in section 1222(9)).

(4) Interest related to exempt-interest dividends

Interest on indebtedness incurred or continued to purchase or carry shares of stock of a regulated investment company which during the taxable year of the holder thereof distributes exempt-interest dividends.

(5) Special rules for application of paragraph (2) in the case of short sales

For purposes of paragraph (2)—

(A) In general

The term “interest” includes any amount paid or incurred—

- (i) by any person making a short sale in connection with personal property used in such short sale, or
- (ii) by any other person for the use of any collateral with respect to such short sale.

(B) Exception where no return on cash collateral

If—

(i) the taxpayer provides cash as collateral for any short sale, and

(ii) the taxpayer receives no material earnings on such cash during the period of the sale,

subparagraph (A)(i) shall not apply to such short sale.

(6) Section not to apply with respect to parsonage and military housing allowances

No deduction shall be denied under this section for interest on a mortgage on, or real property taxes on, the home of the taxpayer by reason of the receipt of an amount as—

(A) a military housing allowance, or

(B) a parsonage allowance excludable from gross income under section 107.

(b) Pro rata allocation of interest expense of financial institutions to tax-exempt interest

(1) In general

In the case of a financial institution, no deduction shall be allowed for that portion of the taxpayer's interest expense which is allocable to tax-exempt interest.

(2) Allocation

For purposes of paragraph (1), the portion of the taxpayer's interest expense which is allocable to tax-exempt interest is an amount which bears the same ratio to such interest expense as—

(A) the taxpayer's average adjusted bases (within the meaning of section 1016) of tax-exempt obligations acquired after August 7, 1986, bears to

(B) such average adjusted bases for all assets of the taxpayer.

(3) Exception for certain tax-exempt obligations

(A) In general

Any qualified tax-exempt obligation acquired after August 7, 1986, shall be treated for purposes of paragraph (2) and section 291(e)(1)(B) as if it were acquired on August 7, 1986.

(B) Qualified tax-exempt obligation

(i) In general

For purposes of subparagraph (A), the term “qualified tax-exempt obligation” means a tax-exempt obligation—

(I) which is issued after August 7, 1986, by a qualified small issuer,

(II) which is not a private activity bond (as defined in section 141), and

(III) which is designated by the issuer for purposes of this paragraph.

(ii) Certain bonds not treated as private activity bonds

For purposes of clause (i)(II), there shall not be treated as a private activity bond—

(I) any qualified 501(c)(3) bond (as defined in section 145), or

(II) any obligation issued to refund (or which is part of a series of obligations issued to refund) an obligation issued before August 8, 1986, which was not an industrial development bond (as defined in section 103(b)(2) as in effect on the day

before the date of the enactment of the Tax Reform Act of 1986) or a private loan bond (as defined in section 103(o)(2)(A), as so in effect, but without regard to any exemption from such definition other than section 103(o)(2)(A)).

(C) Qualified small issuer

(i) In general

For purposes of subparagraph (B), the term “qualified small issuer” means, with respect to obligations issued during any calendar year, any issuer if the reasonably anticipated amount of tax-exempt obligations (other than obligations described in clause (ii)) which will be issued by such issuer during such calendar year does not exceed \$10,000,000.

(ii) Obligations not taken into account in determining status as qualified small issuer

For purposes of clause (i), an obligation is described in this clause if such obligation is—

(I) a private activity bond (other than a qualified 501(c)(3) bond, as defined in section 145),

(II) an obligation to which section 141(a) does not apply by reason of section 1312, 1313, 1316(g), or 1317 of the Tax Reform Act of 1986 and which would (if issued on August 15, 1986) have been an industrial development bond (as defined in section 103(b)(2) as in effect on the day before the date of the enactment of such Act) or a private loan bond (as defined in section 103(o)(2)(A), as so in effect, but without regard to any exception from such definition other than section 103(o)(2)(A)), or

(III) an obligation issued to refund (other than to advance refund within the meaning of section 149(d)(5))¹ any obligation to the extent the amount of the refunding obligation does not exceed the outstanding amount of the refunded obligation.

(iii) Allocation of amount of issue in certain cases

In the case of an issue under which more than 1 governmental entity receives benefits, if—

(I) all governmental entities receiving benefits from such issue irrevocably agree (before the date of issuance of the issue) on an allocation of the amount of such issue for purposes of this subparagraph, and

(II) such allocation bears a reasonable relationship to the respective benefits received by such entities,

then the amount of such issue so allocated to an entity (and only such amount with respect to such issue) shall be taken into account under clause (i) with respect to such entity.

(D) Limitation on amount of obligations which may be designated

(i) In general

Not more than \$10,000,000 of obligations issued by an issuer during any calendar year may be designated by such issuer for purposes of this paragraph.

(ii) Certain refundings of designated obligations deemed designated

Except as provided in clause (iii), in the case of a refunding (or series of refundings) of a qualified tax-exempt obligation, the refunding obligation shall be treated as a qualified tax-exempt obligation (and shall not be taken into account under clause (i)) if—

(I) the refunding obligation was not taken into account under subparagraph (C) by reason of clause (ii)(III) thereof,

(II) the average maturity date of the refunding obligations issued as part of the issue of which such refunding obligation is a part is not later than the average maturity date of the obligations to be refunded by such issue, and

(III) the refunding obligation has a maturity date which is not later than the date which is 30 years after the date the original qualified tax-exempt obligation was issued.

Subclause (II) shall not apply if the average maturity of the issue of which the original qualified tax-exempt obligation was a part (and of the issue of which the obligations to be refunded are a part) is 3 years or less. For purposes of this clause, average maturity shall be determined in accordance with section 147(b)(2)(A).

(iii) Certain obligations may not be designated or deemed designated

No obligation issued as part of an issue may be designated under this paragraph (or may be treated as designated under clause (ii)) if—

(I) any obligation issued as part of such issue is issued to refund another obligation, and

(II) the aggregate face amount of such issue exceeds \$10,000,000.

(E) Aggregation of issuers

For purposes of subparagraphs (C) and (D)—

(i) an issuer and all entities which issue obligations on behalf of such issuer shall be treated as 1 issuer,

(ii) all obligations issued by a subordinate entity shall, for purposes of applying subparagraphs (C) and (D) to each other entity to which such entity is subordinate, be treated as issued by such other entity, and

(iii) an entity formed (or, to the extent provided by the Secretary, availed of) to avoid the purposes of subparagraph (C) or (D) and all entities benefiting thereby shall be treated as 1 issuer.

(F) Treatment of composite issues

In the case of an obligation which is issued as part of a direct or indirect composite

¹ See References in Text note below.

issue, such obligation shall not be treated as a qualified tax-exempt obligation unless—

(i) the requirements of this paragraph are met with respect to such composite issue (determined by treating such composite issue as a single issue), and

(ii) the requirements of this paragraph are met with respect to each separate lot of obligations which are part of the issue (determined by treating each such separate lot as a separate issue).

(G) Special rules for obligations issued during 2009 and 2010

(i) Increase in limitation

In the case of obligations issued during 2009 or 2010, subparagraphs (C)(i), (D)(i), and (D)(iii)(II) shall each be applied by substituting “\$30,000,000” for “\$10,000,000”.

(ii) Qualified 501(c)(3) bonds treated as issued by exempt organization

In the case of a qualified 501(c)(3) bond (as defined in section 145) issued during 2009 or 2010, this paragraph shall be applied by treating the 501(c)(3) organization for whose benefit such bond was issued as the issuer.

(iii) Special rule for qualified financings

In the case of a qualified financing issue issued during 2009 or 2010—

(I) subparagraph (F) shall not apply, and

(II) any obligation issued as a part of such issue shall be treated as a qualified tax-exempt obligation if the requirements of this paragraph are met with respect to each qualified portion of the issue (determined by treating each qualified portion as a separate issue which is issued by the qualified borrower with respect to which such portion relates).

(iv) Qualified financing issue

For purposes of this subparagraph, the term “qualified financing issue” means any composite, pooled, or other conduit financing issue the proceeds of which are used directly or indirectly to make or finance loans to 1 or more ultimate borrowers each of whom is a qualified borrower.

(v) Qualified portion

For purposes of this subparagraph, the term “qualified portion” means that portion of the proceeds which are used with respect to each qualified borrower under the issue.

(vi) Qualified borrower

For purposes of this subparagraph, the term “qualified borrower” means a borrower which is a State or political subdivision thereof or an organization described in section 501(c)(3) and exempt from taxation under section 501(a).

(4) Definitions

For purposes of this subsection—

(A) Interest expense

The term “interest expense” means the aggregate amount allowable to the taxpayer

as a deduction for interest for the taxable year (determined without regard to this subsection, section 264, and section 291). For purposes of the preceding sentence, the term “interest” includes amounts (whether or not designated as interest) paid in respect of deposits, investment certificates, or withdrawable or repurchasable shares.

(B) Tax-exempt obligation

The term “tax-exempt obligation” means any obligation the interest on which is wholly exempt from taxes imposed by this subtitle. Such term includes shares of stock of a regulated investment company which during the taxable year of the holder thereof distributes exempt-interest dividends.

(5) Financial institution

For purposes of this subsection, the term “financial institution” means any person who—

(A) accepts deposits from the public in the ordinary course of such person’s trade or business, and is subject to Federal or State supervision as a financial institution, or

(B) is a corporation described in section 585(a)(2).

(6) Special rules

(A) Coordination with subsection (a)

If interest on any indebtedness is disallowed under subsection (a) with respect to any tax-exempt obligation—

(i) such disallowed interest shall not be taken into account for purposes of applying this subsection, and

(ii) for purposes of applying paragraph (2), the adjusted basis of such tax-exempt obligation shall be reduced (but not below zero) by the amount of such indebtedness.

(B) Coordination with section 263A

This section shall be applied before the application of section 263A (relating to capitalization of certain expenses where taxpayer produces property).

(7) De minimis exception for bonds issued during 2009 or 2010

(A) In general

In applying paragraph (2)(A), there shall not be taken into account tax-exempt obligations issued during 2009 or 2010.

(B) Limitation

The amount of tax-exempt obligations not taken into account by reason of subparagraph (A) shall not exceed 2 percent of the amount determined under paragraph (2)(B).

(C) Refundings

For purposes of this paragraph, a refunding bond (whether a current or advance refunding) shall be treated as issued on the date of the issuance of the refunded bond (or in the case of a series of refundings, the original bond).

(Aug. 16, 1954, ch. 736, 68A Stat. 78; Pub. L. 88–272, title II, §216(a), Feb. 26, 1964, 78 Stat. 56; Pub. L. 94–455, title XIX, §§1901(a)(37), 1906(b)(13)(A), title XXI, §2137(e), Oct. 4, 1976, 90 Stat. 1770, 1834,

1931; Pub. L. 96-223, title IV, §404(b)(2), Apr. 2, 1980, 94 Stat. 306; Pub. L. 97-34, title III, §§301(b)(2), 302(c)(2), (d)(1), Aug. 13, 1981, 95 Stat. 270, 272, 274; Pub. L. 98-369, div. A, title I, §§16(a), 56(c), July 18, 1984, 98 Stat. 505, 574; Pub. L. 99-514, title I, §144, title IX, §902(a), (b), (d), Oct. 22, 1986, 100 Stat. 2121, 2380-2382; Pub. L. 100-647, title I, §1009(b)(3)(A), Nov. 10, 1988, 102 Stat. 3446; Pub. L. 101-508, title XI, §11801(c)(4), Nov. 5, 1990, 104 Stat. 1388-523; Pub. L. 105-34, title X, §1084(c), Aug. 5, 1997, 111 Stat. 955; Pub. L. 111-5, div. B, title I, §§1501(a), 1502(a), Feb. 17, 2009, 123 Stat. 353.)

Editorial Notes

REFERENCES IN TEXT

The date of the enactment of the Tax Reform Act of 1986, referred to in subsec. (b)(3)(B)(ii)(II), (C)(ii)(II), is the date of enactment of Pub. L. 99-514, which was approved Oct. 22, 1986.

Sections 1312, 1313, 1316(g), and 1317 of the Tax Reform Act of 1986, referred to in subsec. (b)(3)(C)(ii)(II), are sections 1312, 1313, 1316(g), and 1317 of Pub. L. 99-514, which are set out as a note under section 141 of this title.

Section 149(d)(5), referred to in subsec. (b)(3)(C)(ii)(III), was redesignated section 149(d)(2) by Pub. L. 115-97, title I, §13532(b)(1), Dec. 22, 2017, 131 Stat. 2154.

CODIFICATION

Another section 1084(c) of Pub. L. 105-34 amended section 264 of this title.

AMENDMENTS

2009—Subsec. (b)(3)(G). Pub. L. 111-5, §1502(a), added subpar. (G).

Subsec. (b)(7). Pub. L. 111-5, §1501(a), added par. (7).

1997—Subsec. (b)(4)(A). Pub. L. 105-34 inserted “, section 264,” before “and section 291”.

1990—Subsec. (a)(2). Pub. L. 101-508, §11801(c)(4), struck out before period at end “, or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128”.

1988—Subsec. (b)(3). Pub. L. 100-647 amended par. (3) generally, reenacting subpar. (A) without change, revising and restating provisions of subpars. (B) to (E), and adding subpar. (F).

1986—Pub. L. 99-514, §902(a), (d), designated existing provisions as subsec. (a), inserted heading, and added subsec. (b).

Par. (2). Pub. L. 99-514, §902(b), struck out last sentence which read as follows: “In applying the preceding sentence to a financial institution (other than a bank) which is a face-amount certificate company registered under the Investment Company Act of 1940 (15 U.S.C. 80a-1 and following) and which is subject to the banking laws of the State in which such institution is incorporated, interest on face-amount certificates (as defined in section 2(a)(15) of such Act) issued by such institution, and interest on amounts received for the purchase of such certificates to be issued by such institution, shall not be considered as interest on indebtedness incurred or continued to purchase or carry obligations the interest on which is wholly exempt from the taxes imposed by this subtitle, to the extent that the average amount of such obligations held by such institution during the taxable year (as determined under regulations prescribed by the Secretary) does not exceed 15 percent of the average of the total assets held by such institution during the taxable year (as so determined).”

Par. (6). Pub. L. 99-514, §144, added par. (6).

1984—Par. (2). Pub. L. 98-369, §16(a), repealed amendments made by Pub. L. 97-34, §302(c). See 1981 Amendment note below.

Par. (5). Pub. L. 98-369, §56(c), added par. (5).

1981—Par. (2). Pub. L. 97-34, §302(c)(2), (d)(1), provided that, applicable to taxable years beginning after Dec. 31, 1984, par. (2) is amended by striking out “or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128” and inserting in lieu thereof “or to purchase or carry obligations or shares, or to make other deposits or investments, the interest on which is described in section 128(c)(1) to the extent such interest is excludable from gross income under section 128”. Section 16(a) of Pub. L. 98-369, repealed section 302(c) of Pub. L. 97-34, and provided that this title shall be applied and administered as if section 302(c), and the amendments made by such section 302(c), had not been enacted.

Pub. L. 97-34, §301(b)(2), inserted “, or to purchase or carry any certificate to the extent the interest on such certificate is excludable under section 128” after “116”.

1980—Par. (2). Pub. L. 96-223 inserted “, or to purchase or carry obligations or shares, or to make deposits or other investments, the interest on which is described in section 116(c) to the extent such interest is excludable from gross income under section 116” after “subtitle”.

1976—Par. (2). Pub. L. 94-455, §§1901(a)(37), 1906(b)(13)(A), struck out “(other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer)” after “to purchase or carry obligations” and “or his delegate” after “Secretary”.

Pars. (3), (4). Pub. L. 94-455, §2137(e), added pars. (3) and (4).

1964—Par. (2). Pub. L. 88-272 provided that interest on face-amount certificates issued by a face-amount certificate company, and interest on amounts received for the purchase of such certificates to be issued by such institution, shall not be considered interest on indebtedness to purchase or carry obligations the interest on which is wholly exempt from the taxes under this subtitle, to the extent the average amount of such obligations held by such institution during the taxable year doesn't exceed 15 percent of the average total assets held by such institution during the taxable year.

Statutory Notes and Related Subsidiaries

EFFECTIVE DATE OF 2009 AMENDMENT

Pub. L. 111-5, div. B, title I, §1501(c), Feb. 17, 2009, 123 Stat. 353, provided that: “The amendments made by this section [amending this section and section 291 of this title] shall apply to obligations issued after December 31, 2008.”

Pub. L. 111-5, div. B, title I, §1502(b), Feb. 17, 2009, 123 Stat. 354, provided that: “The amendment made by this section [amending this section] shall apply to obligations issued after December 31, 2008.”

EFFECTIVE DATE OF 1997 AMENDMENT

Amendment by Pub. L. 105-34 applicable to contracts issued after June 8, 1997, in taxable years ending after such date, with special provisions relating to changes in contracts to be treated as new contracts, see section 1084(d) of Pub. L. 105-34, set out as a note under section 101 of this title.

EFFECTIVE DATE OF 1988 AMENDMENT

Pub. L. 100-647, title I, §1009(b)(3)(B)–(D), Nov. 10, 1988, 102 Stat. 3448, 3449, as amended by Pub. L. 101-239, title VII, §7811(f)(2), Dec. 19, 1989, 103 Stat. 2409, provided that:

“(B) In the case of any obligation issued after August 7, 1986, and before January 1, 1987, the time for making a designation with respect to such obligation under section 265(b)(3)(B)(i)(III) of the 1986 Code shall not expire before January 1, 1989.

“(C) If—

“(i) an obligation is issued on or after January 1, 1986, and on or before August 7, 1986,

“(ii) when such obligation was issued, the issuer made a designation that it intended to qualify under

section 802(e)(3) of H.R. 3838 of the 99th Congress as passed by the House of Representatives [H.R. 3838 was enacted as Pub. L. 99-514], and

“(iii) the issuer makes an election under this subparagraph with respect to such obligation, for purposes of section 265(b)(3) of the 1986 Code, such obligation shall be treated as issued on August 8, 1986.

“(D)(i) Except as provided in clause (ii), the following provisions of section 265(b)(3) of the 1986 Code (as amended by this subparagraph (A)) shall apply to obligations issued after June 30, 1987:

“(I) subparagraph (C)(ii)(III),

“(II) clauses (i) and (iii) of subparagraph (D), and

“(III) subparagraphs (E) and (F).

“(ii) At the election of an issuer (made at such time and in such manner as the Secretary of the Treasury or his delegate may prescribe), the provisions referred to in clause (i) shall apply to such issuer as if included in the amendments made by section 902(a) of the Tax Reform Act of 1986 [section 902(a) of Pub. L. 99-514, amending this section].”

Amendment by 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.

EFFECTIVE DATE OF 1986 AMENDMENT

Amendment by section 144 of Pub. L. 99-514 applicable to taxable years beginning before, on, or after Dec. 31, 1986, see section 151(e) of Pub. L. 99-514, set out as a note under section 1 of this title.

Pub. L. 99-514, title IX, §902(f), Oct. 22, 1986, 100 Stat. 2382, as amended by Pub. L. 100-647, title I, §1009(b)(1), (2), (7), Nov. 10, 1988, 102 Stat. 3445, 3446, 3449, provided that:

“(1) IN GENERAL.—Except as provided in this subsection, the amendments made by this section [amending this section and sections 163, 291, and 1277 of this title] shall apply to taxable years ending after December 31, 1986.

“(2) OBLIGATIONS ACQUIRED PURSUANT TO CERTAIN COMMITMENTS.—For purposes of sections 265(b) and 291(e)(1)(B) of the Internal Revenue Code of 1986, any tax-exempt obligation which is acquired after August 7, 1986, pursuant to a direct or indirect written commitment—

“(A) to purchase or repurchase such obligation, and

“(B) entered into on or before September 25, 1985, shall be treated as an obligation acquired before August 8, 1986.

“(3) TRANSITIONAL RULES.—For purposes of sections 265(b) and 291(e)(1)(B) of the Internal Revenue Code of 1986, obligations with respect to any of the following projects shall be treated as obligations acquired before August 8, 1986, in the hands of the first and any subsequent financial institution acquiring such obligations:

“(A) Park Forest, Illinois, redevelopment project.

“(B) Clinton, Tennessee, Carriage Trace project.

“(C) Savannah, Georgia, Mall Terrace Warehouse project.

“(D) Chattanooga, Tennessee, Warehouse Row project.

“(E) Dalton, Georgia, Towne Square project.

“(F) Milwaukee, Wisconsin, Standard Electric Supply Company—distribution facility.

“(G) Wausau, Wisconsin, urban renewal project.

“(H) Cassville, Missouri, UDAG project.

“(I) Outlook Envelope Company—plant expansion.

“(J) Woodstock, Connecticut, Crabtree Warehouse partnership.

“(K) Louisville, Kentucky, Speed Mansion renovation project.

“(L) Charleston, South Carolina, 2 Festival Market Place projects at Union Pier Terminal and 1 project at the Remount Road Container Yard, State Pier No. 15 at North Charleston Terminal.

“(M) New Orleans, Louisiana, Upper Pontalba Building renovation.

“(N) Woodward Wight Building.

“(O) Minneapolis, Minnesota, Miller Milling Company—flour mill project.

“(P) Homewood, Alabama, the Club Apartments.

“(Q) Charlotte, North Carolina—qualified mortgage bonds acquired by NCNB bank (\$5,250,000).

“(R) Grand Rapids, Michigan, Central Bank project.

“(S) Ruppman Marketing Services, Inc.—building project.

“(T) Bellows Falls, Vermont—building project.

“(U) East Broadway Project, Louisville, Kentucky.

“(V) O.K. Industries, Oklahoma.

“(4) ADDITIONAL TRANSITIONAL RULE.—Obligations issued pursuant to an allocation of a State's volume limitation for private activity bonds, which allocation was made by Executive Order 25 signed by the Governor of the State on May 22, 1986 (as such order may be amended before January 1, 1987), and qualified 501(c)(3) bonds designated by such Governor for purposes of this paragraph, shall be treated as acquired on or before August 7, 1986, in the hands of the first and any subsequent financial institution acquiring such obligation. The aggregate face amount of obligations to which this paragraph applies shall not exceed \$200,000,000.”

EFFECTIVE DATE OF 1984 AMENDMENT

Amendment by section 16(a) of Pub. L. 98-369 applicable to taxable years ending after Dec. 31, 1983, see section 18(a) of Pub. L. 98-369, set out as a note under section 48 of this title.

Amendment by section 56(c) of Pub. L. 98-369 applicable to short sales after July 18, 1984, in taxable years ending after that date, see section 56(d) of Pub. L. 98-369, set out as a note under section 163 of this title.

EFFECTIVE DATE OF 1981 AMENDMENT

Pub. L. 97-34, title III, §301(d), Aug. 13, 1981, 95 Stat. 270, provided that:

“(1) IN GENERAL.—Except as provided in paragraph (2), the amendments made by this section [enacting section 128 of this title and amending this section and sections 584, 643, and 702 of this title] shall apply to taxable years ending after September 30, 1981.

“(2) CONFORMING AMENDMENTS.—The amendments made by subsection (b)(6) [amending sections 584, 643, and 702 of this title] shall apply to taxable years beginning after December 31, 1981.”

EFFECTIVE AND TERMINATION DATES OF 1980 AMENDMENT

Pub. L. 96-223, title IV, §404(c), Apr. 2, 1980, 94 Stat. 308, as amended by Pub. L. 97-34, title III, §302(b)(1), Aug. 13, 1981, 95 Stat. 272, provided that: “The amendments made by this section [amending this section and sections 116, 584, 643, 702, 854, and 857 of this title] shall apply with respect to taxable years beginning after December 31, 1980, and before January 1, 1982.”

EFFECTIVE DATE OF 1976 AMENDMENT

Amendment by section 1901(a)(37) of Pub. L. 94-455 effective for taxable years beginning after Dec. 31, 1976, see section 1901(d) of Pub. L. 94-455, set out as a note under section 2 of this title.

Amendment by section 2137(e) of Pub. L. 94-455 effective for taxable years beginning after Dec. 31, 1975, see section 2137(e) of Pub. L. 94-455, set out as a note under section 852 of this title.

EFFECTIVE DATE OF 1964 AMENDMENT

Pub. L. 88-272, title II, §216(b), Feb. 26, 1964, 78 Stat. 56, provided that: “The amendment made by subsection (a) [amending this section] shall apply with respect to taxable years ending after the date of the enactment of this Act [Feb. 26, 1964].”

SAVINGS PROVISION

For provisions that nothing in amendment by Pub. L. 101-508 be construed to affect treatment of certain transactions occurring, property acquired, or items of

income, loss, deduction, or credit taken into account prior to Nov. 5, 1990, for purposes of determining liability for tax for periods ending after Nov. 5, 1990, see section 11821(b) of Pub. L. 101-508, set out as a note under section 45K of this title.

CLARIFICATION OF TREATMENT OF AMOUNTS EXCLUDED
UNDER SECTION 597

Pub. L. 99-514, title IX, §904(c)(2)(B), Oct. 22, 1986, 100 Stat. 2385, provided that this section shall not deny any deduction by reason of such deduction being allocable to amounts excluded from gross income under section 597 of this title as in effect on Oct. 21, 1986, prior to repeal by Pub. L. 101-73, title XIV, §1401(a)(3)(B), Aug. 9, 1989, 103 Stat. 549.

§ 266. Carrying charges

No deduction shall be allowed for amounts paid or accrued for such taxes and carrying charges as, under regulations prescribed by the Secretary, are chargeable to capital account with respect to property, if the taxpayer elects, in accordance with such regulations, to treat such taxes or charges as so chargeable.

(Aug. 16, 1954, ch. 736, 68A Stat. 78; Pub. L. 94-455, title XIX, §1906(b)(13)(A), Oct. 4, 1976, 90 Stat. 1834.)

Editorial Notes

AMENDMENTS

1976—Pub. L. 94-455 struck out “or his delegate” after “Secretary”.

§ 267. Losses, expenses, and interest with respect to transactions between related taxpayers

(a) In general

(1) Deduction for losses disallowed

No deduction shall be allowed in respect of any loss from the sale or exchange of property, directly or indirectly, between persons specified in any of the paragraphs of subsection (b). The preceding sentence shall not apply to any loss of the distributing corporation (or the distributee) in the case of a distribution in complete liquidation.

(2) Matching of deduction and payee income item in the case of expenses and interest

If—

(A) by reason of the method of accounting of the person to whom the payment is to be made, the amount thereof is not (unless paid) includible in the gross income of such person, and

(B) at the close of the taxable year of the taxpayer for which (but for this paragraph) the amount would be deductible under this chapter, both the taxpayer and the person to whom the payment is to be made are persons specified in any of the paragraphs of subsection (b),

then any deduction allowable under this chapter in respect of such amount shall be allowable as of the day as of which such amount is includible in the gross income of the person to whom the payment is made (or, if later, as of the day on which it would be so allowable but for this paragraph). For purposes of this paragraph, in the case of a personal service corporation (within the meaning of section

441(i)(2)), such corporation and any employee-owner (within the meaning of section 269A(b)(2), as modified by section 441(i)(2)) shall be treated as persons specified in subsection (b).

(3) Payments to foreign persons

(A) In general

The Secretary shall by regulations apply the matching principle of paragraph (2) in cases in which the person to whom the payment is to be made is not a United States person.

(B) Special rule for certain foreign entities

(i) In general

Notwithstanding subparagraph (A), in the case of any item payable to a controlled foreign corporation (as defined in section 957) or a passive foreign investment company (as defined in section 1297), a deduction shall be allowable to the payor with respect to such amount for any taxable year before the taxable year in which paid only to the extent that an amount attributable to such item is includible (determined without regard to properly allocable deductions and qualified deficits under section 952(c)(1)(B)) during such prior taxable year in the gross income of a United States person who owns (within the meaning of section 958(a)) stock in such corporation.

(ii) Secretarial authority

The Secretary may by regulation exempt transactions from the application of clause (i), including any transaction which is entered into by a payor in the ordinary course of a trade or business in which the payor is predominantly engaged and in which the payment of the accrued amounts occurs within 8½ months after accrual or within such other period as the Secretary may prescribe.

(b) Relationships

The persons referred to in subsection (a) are:

(1) Members of a family, as defined in subsection (c)(4);

(2) An individual and a corporation more than 50 percent in value of the outstanding stock of which is owned, directly or indirectly, by or for such individual;

(3) Two corporations which are members of the same controlled group (as defined in subsection (f));

(4) A grantor and a fiduciary of any trust;

(5) A fiduciary of a trust and a fiduciary of another trust, if the same person is a grantor of both trusts;

(6) A fiduciary of a trust and a beneficiary of such trust;

(7) A fiduciary of a trust and a beneficiary of another trust, if the same person is a grantor of both trusts;

(8) A fiduciary of a trust and a corporation more than 50 percent in value of the outstanding stock of which is owned, directly or indirectly, by or for the trust or by or for a person who is a grantor of the trust;

(9) A person and an organization to which section 501 (relating to certain educational