

Rules and Regulations

Title 5—ADMINISTRATIVE PERSONNEL

Chapter I—Civil Service Commission PART 733—POLITICAL ACTIVITIES OF FEDERAL EMPLOYEES

Subpart C—Privileged Localities

MONTGOMERY COUNTY, MARYLAND

Section 733.301 is amended to grant an exception from the prohibitions of section 9 of the Hatch Political Activities Act to employee residents of Montgomery County, Maryland. Section 733.301(b) is amended by the addition of "Montgomery County (April 30, 1964)" under the heading "In Maryland".

(R.S. 1753, sec. 2, 22 Stat. 403, as amended; 5 U.S.C. 631, 633; E.O. 10577, 19 F.R. 7521, 3 CFR, 1954-1958 Comp., p. 218)

UNITED STATES CIVIL SERVICE COMMISSION,

[SEAL] MARY V. WENZEL,
Executive Assistant to
the Commissioners.

[F.R. Doc. 64-4621; Filed, May 7, 1964;
8:47 a.m.]

Title 12—BANKS AND BANKING

Chapter II—Federal Reserve System

SUBCHAPTER A—BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. H]

PART 208—MEMBERSHIP OF STATE BANKING INSTITUTIONS IN THE FEDERAL RESERVE SYSTEM

Underwriting of Public Authority Bonds

§ 208.109 Underwriting of public Authority bonds payable from rents under lease with governmental entity having general taxing powers.

(a) The Board of Governors has been asked whether securities of a public Authority that are to be paid from rents payable under a lease of the Authority's facilities to a governmental entity that possesses general powers of taxation, including property taxation, constitute "general obligations" within the meaning of section 5136 of the United States Revised Statutes (12 U.S.C. 24). In cases where this question can be answered in the affirmative, member State banks of the Federal Reserve System may lawfully underwrite and deal in such securities, and invest therein without limitation on amount, as far as Federal banking law is concerned.

(b) The Board understands that the issuing Authorities usually have no taxing powers and that their obligations are not, under pertinent State constitutional

and statutory provisions as interpreted by the courts, "debts" of the lessee—that is, the governmental entity with general powers of taxation. However, whether a security constitutes a "debt" for purposes of State law is not determinative as to whether it is a "general obligation" within the meaning of section 5136, a Federal statute. (See § 208.105, 28 F.R. 9840.)

(c) During recent Hearings before the Committee on Banking and Currency of the House of Representatives, published under the title "Increased Flexibility for Financial Institutions—1963", the Board expressed its understanding of the meaning of the phrase "general obligations of any State or of any political subdivision thereof" as used in section 5136.

(d) As the House Committee was informed, the Board understands that phrase to include "only obligations that are supported by an unconditional promise to pay, directly or indirectly, an aggregate amount which (together with any other funds available for the purpose) will suffice to discharge, when due, all interest on and principal of such obligations, which promise (1) is made by a Governmental entity that possesses general powers of taxation, including property taxation, and (2) pledges or otherwise commits the full faith and credit of said promisor; said term does not include obligations not so supported that are to be repaid only from specified sources such as the income from designated facilities or the proceeds of designated taxes." (Hearings, p. 1018.)

(e) A major requirement of the foregoing definition is that a "general obligation" must be supported by general powers of taxation, including property taxation. The Board recognizes, however, that such support by general powers of taxation may be indirect as well as direct.

(f) If a State (or other governmental entity having general powers of taxation) agrees unconditionally to pay to an Authority rentals that will be sufficient and will be used, in all events, to cover required payments of interest and principal on the relevant securities when due, the securities, in the opinion of the Board, are indirectly supported by general taxing powers, and, accordingly, constitute "general obligations" within the meaning of R.S. 5136. On the other hand, if the lease does not contain an unconditional promise of the State to provide sums sufficient, in all events, to cover required payments of interest and principal on the bonds of the lessor Authority as they become due, the securities cannot be considered "general obligations".

(g) The status of a particular issue of such lease-supported bonds thus depends upon the terms of the lease involved. Where the lease is for a term of years not less than the maximum maturity of the relevant bond issue, and the State

unconditionally promises to pay rentals sufficient to cover all payments on the bonds as they become due, the bonds ordinarily will qualify as "general obligations". Where the promise of the State is to pay a fixed dollar rental, the securities will not qualify as "general obligations" unless the lease provides that rental payments in amounts sufficient to service the bonds cannot be expended by the authority for any other purpose than the payment of principal and interest thereon.

(h) This interpretation is intended to indicate the circumstances in which securities issued by public Authorities without taxing powers constitute "general obligations" that are eligible for underwriting by member banks, under R.S. 5136. The status of any particular issue can only be determined through examination of all relevant laws and contracts, in order to ascertain the actual legal and financial arrangements.

(12 U.S.C. 248(1). Interprets 12 U.S.C. 24 and 335)

Dated at Washington, D.C., this 30th day of April, 1964.

BOARD OF GOVERNORS OF THE
FEDERAL RESERVE SYSTEM,

[SEAL] MERRITT SHERMAN,
Secretary.

[F.R. Doc. 64-4598; Filed, May 7, 1964;
8:45 a.m.]

Title 14—AERONAUTICS AND SPACE

Chapter I—Federal Aviation Agency

SUBCHAPTER E—AIRSPACE [NEW]

[Airspace Docket No. 63-SO-48]

PART 73—SPECIAL USE AIRSPACE [NEW]

Valparaiso, Fla.; Correction

On April 1, 1964, F.R. Doc. 64-3126 was published in the FEDERAL REGISTER (29 F.R. 4670) and in part altered R-2915 Valparaiso, Fla., by dividing it into two parts, R-2915A and R-2915B.

In Item 1c R-2915B was incorrectly cited as R-2615B. Corrective action is taken herein.

Since this change is editorial in nature and imposes no additional burden on any person, compliance with section 4 of the Administrative Procedure Act is unnecessary and the effective date as initially adopted may be retained.

In consideration of the foregoing, effective immediately, F.R. Doc. 64-3126 (29 F.R. 4670) is altered as follows: In the caption of Item 1c "R-2615B" is deleted and "R-2915B" is substituted therefor.

(Sec. 307(a), 72 Stat. 749; 49 U.S.C. 1348)

Issued in Washington, D.C., on April 29, 1964.

LEE E. WARREN,
Director, Air Traffic Service.

[F.R. Doc. 64-4599; Filed, May 7, 1964;
8:45 a.m.]

[Airspace Docket No. 64-SO-6]

PART 73—SPECIAL USE AIRSPACE [NEW]

Alteration of Restricted Area

The purpose of this amendment to § 73.29 of the Federal Aviation Regulations is to reduce the designated altitudes of the Avon Park West, Fla., Restricted Area R-2901C from "Surface to flight level 400" to "Surface to flight level 240."

The Department of the Air Force has advised the Federal Aviation Agency that their activities in R-2901C can be conducted below flight level 240. Accordingly, action is taken herein to change the designated altitudes of R-2901C to "Surface to flight level 240."

Since this amendment reduces a burden on the public, compliance with notice, public procedure and effective date requirements of section 4 of the Administrative Procedure Act is unnecessary and it may be made effective upon publication.

In consideration of the foregoing, the following action is taken: In § 73.29 (29 F.R. 1245), R-2901C Avon Park West, Fla., "Designated altitudes. Surface to flight level 400." is deleted and "Designated altitudes. Surface to flight level 240." is substituted therefor.

This amendment shall become effective upon the date of publication in the FEDERAL REGISTER.

(Sec. 307(a), 72 Stat. 749; 49 U.S.C. 1348)

Issued in Washington, D.C., on April 29, 1964.

LEE E. WARREN,
Director, Air Traffic Service.

[F.R. Doc. 64-4600; Filed, May 7, 1964;
8:45 a.m.]

[Airspace Docket No. 64-SO-9]

PART 73—SPECIAL USE AIRSPACE [NEW]

Alteration of Restricted Area

The purpose of this amendment to § 73.60 of the Federal Aviation Regulations is to designate the Fort Jackson, S.C., Restricted Area R-6001 as a joint use area with the Jacksonville ARTC Center as controlling agency. This action would result in more efficient utilization of the airspace within R-6001 and has Department of Army concurrence.

Since this amendment reduces a burden on the public, compliance with the notice, public procedure and effective date requirements of section 4 of the Administrative Procedure Act is unnecessary and it may be made effective on publication.

In consideration of the foregoing, the following action is taken: In the text § 73.60 (29 F.R. 1275), R-6001 Fort Jack-

son, S.C., "Using agency. Commanding General, Fort Jackson, S.C." is deleted and "Controlling agency. Federal Aviation Agency, Jacksonville ARTC Center. Using agency. Commanding General, Fort Jackson, S.C." is substituted therefor.

(Sec. 307(a), 72 Stat. 749; 49 U.S.C. 1348)

This amendment shall become effective upon the date of publication in the FEDERAL REGISTER.

Issued in Washington, D.C., on April 29, 1964.

LEE E. WARREN,
Director, Air Traffic Service.

[F.R. Doc. 64-4601; Filed May 7, 1964;
8:46 a.m.]

Title 21—FOOD AND DRUGS

Chapter I—Food and Drug Administration, Department of Health, Education, and Welfare

SUBCHAPTER C—DRUGS

PART 146a—CERTIFICATION OF PENICILLIN AND PENICILLIN-CONTAINING DRUGS

Sterility Test Methods and Procedures; Correction

In F.R. Document 64-3043, appearing in the issue for Saturday, March 28, 1964, at page 4119, the amendatory language in amendments numbered 64a, 65a, 66a, 68a, and 70a should be corrected to read: "a. By changing paragraph (d)(3)(i) and (ii) to read:"

Dated: May 1, 1964.

JOHN L. HARVEY,
Deputy Commissioner
of Food and Drugs.

[F.R. Doc. 64-4628; Filed, May 7, 1964;
8:48 a.m.]

Title 26—INTERNAL REVENUE

Chapter I—Internal Revenue Service, Department of the Treasury

SUBCHAPTER A—INCOME TAX

[T. D. 6731]

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Miscellaneous Amendments

On March 28, 1963, notice of proposed rule making with respect to the amendment of the Income Tax Regulations (26 CFR Part 1) to conform the regulations to certain provisions of section 2 of the Revenue Act of 1962 (76 Stat. 962), relating to credit for investment in certain depreciable property, was published in the FEDERAL REGISTER (28 F.R. 3028). After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed, and after taking into account certain pertinent amendments made by the Revenue Act of 1964 (78 Stat. 19), the

amendment of the regulations as proposed is hereby adopted, subject to the changes set forth below. Sections 1.46, 1.46-1, 1.48, and 1.48-4 of the regulations supersede §§ 16.1, 16.1-1, 16.2, and 16.2-1 of Treasury Decision 6619 (26 CFR Part 16), approved November 15, 1962 (27 F.R. 11401).

PARAGRAPH 1. Section 1.46, as set forth in the notice of proposed rule making, is changed by revising subsection (a)(3) of section 46 and by revising the historical note.

PAR. 2. Section 1.46-1, as set forth in the notice of proposed rule making, is changed by revising paragraph (c), and by revising paragraph (f)(2)(i), by adding a new subdivision (iv) to paragraph (f)(2), by revising paragraph (f)(3)(iii), by revising paragraph (f)(6), by revising paragraph (f)(7)(iii), and by revising examples (1) and (4) of paragraph (f)(8).

PAR. 3. Section 1.46-2, as set forth in the notice of proposed rule making, is changed by revising paragraph (g) exclusive of the examples, and by adding to such section a new paragraph (h).

PAR. 4. Section 1.46-3, as set forth in the notice of proposed rule making, is changed by revising subparagraph (1) of paragraph (c), and by revising paragraphs (d) and (e).

PAR. 5. Section 1.46-4, as set forth in the notice of proposed rule making, is changed by revising subparagraphs (2) and (3) of paragraph (b), and by revising subparagraphs (2) and (3) of paragraph (c).

PAR. 6. Section 1.48, as set forth in the notice of proposed rule making, is changed by revising subsections (a)(1) and (d), and by striking out subsection (g), of section 48, and by revising the historical note.

PAR. 7. Section 1.48-1, as set forth in the notice of proposed rule making, is changed by revising paragraphs (a), (b), (c), (f), (g)(2)(ii), (h)(1)(ii), (j), and (k).

PAR. 8. Section 1.48-2, as set forth in the notice of proposed rule making, is changed by revising paragraph (b).

PAR. 9. Section 1.48-3, as set forth in the notice of proposed rule making, is changed by striking out subdivision (iii) of subparagraph (4) of paragraph (c), by revising subparagraph (1)(iii) of paragraph (e), by adding a new subdivision (iv) to paragraph (e)(1), and by revising subparagraphs (2)(ii), (5)(i) and (iii) of paragraph (e).

PAR. 10. Section 1.48-4, as set forth in the notice of proposed rule making, is revised.

PAR. 11. Section 1.48-7, as set forth in the notice of proposed rule making, is changed by revising subparagraph (1) of paragraph (a), and paragraph (b).

(Sec. 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805))

[SEAL] MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved: May 5, 1964.

STANLEY S. SURREY,
Assistant Secretary of the
Treasury.

In order to conform the Income Tax Regulations (26 CFR Part 1) to certain provisions of section 2 of the Revenue Act of 1962 (76 Stat. 962), relating to credit for investment in certain depreciable property, and after taking into account certain pertinent amendments made by the Revenue Act of 1964 (78 Stat. 19), such regulations are amended as set forth below. Sections 1.46, 1.46-1, 1.48, and 1.48-4 of the regulations supersede §§ 16.1, 16.1-1, 16.2, and 16.2-1 of Treasury Decision 6619 (26 CFR Part 16), approved November 15, 1962 (27 F.R. 11401).

- Sec.
- 1.38 Statutory provisions; investment in certain depreciable property.
- 1.39 Statutory provisions; overpayments of tax.
- 1.46 Statutory provisions; amount of credit.
- 1.46-1 Determination of amount.
- 1.46-2 Carryback and carryover of unused credit.
- 1.46-3 Qualified investment.
- 1.46-4 Limitations with respect to certain persons.
- 1.47 Statutory provisions; certain dispositions, etc., of section 38 property.
- 1.47-1 [Reserved]
- 1.48 Statutory provisions; definitions; special rules.
- 1.48-1 Definition of section 38 property.
- 1.48-2 New section 38 property.
- 1.48-3 Used section 38 property.
- 1.48-4 Election of lessor or new section 38 property to treat lessee as purchaser.
- 1.48-5 Electing small business corporations.
- 1.48-6 Estates and trusts.
- 1.48-7 Adjustment to basis.

AUTHORITY: The provisions of these §§ 1.38; 1.39; 1.46 to 1.48-4; 1.47, 1.47-1; 1.48 to 1.48-7; issued under sec. 7805 of the Internal Revenue Code of 1954, 68A Stat. 917; 26 U.S.C. 7805.

PARAGRAPH 1. The following new inferior center heading is inserted after the center heading "Credits Against Tax" which appears immediately preceding § 1.31:

CREDITS ALLOWABLE

PAR. 2. Section 1.38 is redesignated as § 1.39 and there is inserted immediately after § 1.37-5 a new § 1.38. The new and redesignated sections read as follows:

§ 1.38 Statutory provisions; investment in certain depreciable property.

Sec. 38. Investment in certain depreciable property—(a) General rule. There shall be allowed, as a credit against the tax imposed by this chapter, the amount determined under subpart B of this part.

(b) Regulations. The Secretary or his delegate shall prescribe such regulations as may be necessary to carry out the purposes of this section and subpart B.

[Sec. 38 as added by sec. 2(a), Rev. Act 1962 (76 Stat. 962)]

§ 1.39 Statutory provisions; overpayments of tax.

Sec. 39. Overpayments of tax. For credit against the tax imposed by this subtitle for overpayments of tax, see section 6401.

[Sec. 39 as renumbered by sec. 2(a), Rev. Act 1962 (76 Stat. 962)]

PAR. 3. There are inserted immediately after § 1.39 the following new sections:

RULES FOR COMPUTING CREDIT FOR INVESTMENT IN CERTAIN DEPRECIABLE PROPERTY.

§ 1.46 Statutory provisions; amount of credit.

Sec. 46. Amount of credit—(a) Determination of amount—(1) General rule. The amount of the credit allowed by section 38 for the taxable year shall be equal to 7 percent of the qualified investment (as defined in subsection (c)).

(2) Limitation based on amount of tax. Notwithstanding paragraph (1), the credit allowed by section 38 for the taxable year shall not exceed—

(A) So much of the liability for tax for the taxable year as does not exceed \$25,000 plus

(B) 25 percent of so much of the liability for tax for the taxable year as exceeds \$25,000.

(3) Liability for tax. For purposes of paragraph (2), the liability for tax for the taxable year shall be the tax imposed by this chapter for such year, reduced by the sum of the credits allowable under—

(A) Section 33 (relating to foreign tax credit),

(B) Section 35 (relating to partially tax-exempt interest), and

(C) Section 37 (relating to retirement income).

For purposes of this paragraph, any tax imposed for the taxable year by section 531 (relating to accumulated earnings tax) or by section 541 (relating to personal holding company tax) shall not be considered tax imposed by this chapter for such year.

(4) Married individuals. In the case of a husband or wife who files a separate return, the amount specified under subparagraphs (A) and (B) of paragraph (2) shall be \$12,500 in lieu of \$25,000. This paragraph shall not apply if the spouse of the taxpayer has no qualified investment for, and no unused credit carryback or carryover to, the taxable year of such spouse which ends within or with the taxpayer's taxable year.

(5) Affiliated groups. In the case of an affiliated group, the \$25,000 amount specified under subparagraphs (A) and (B) of paragraph (2) shall be reduced for each member of the group by apportioning \$25,000 among the members of such group in such manner as the Secretary or his delegate shall by regulations prescribe. For purposes of the preceding sentence, the term "affiliated group" has the meaning assigned to such term by section 1504(a), except that all corporations shall be treated as includible corporations (without any exclusion under section 1504(b)).

(b) Carryback and carryover of unused credits—(1) Allowance of credit. If the amount of the credit determined under subsection (a)(1) for any taxable year exceeds the limitation provided by subsection (a)(2) for such taxable year (hereinafter in this subsection referred to as "unused credit year"), such excess shall be—

(A) An investment credit carryback to each of the 3 taxable years preceding the unused credit year, and

(B) An investment credit carryover to each of the 5 taxable years following the unused credit year,

and shall be added to the amount allowable as a credit by section 38 for such years, except that such excess may be a carryback only to a taxable year ending after December 31, 1961. The entire amount of the unused credit for an unused credit year shall be carried to the earliest of the 8 taxable years to which (by reason of subparagraphs (A) and (B)) such credit may be carried, and then to each of the other 7 taxable years to the extent that, because of the limitation contained in paragraph (2), such unused credit may not be added for a

prior taxable year to which such unused credit may be carried.

(2) Limitation. The amount of the unused credit which may be added under paragraph (1) for any preceding or succeeding taxable year shall not exceed the amount by which the limitation provided by subsection (a)(2) for such taxable year exceeds the sum of—

(A) The credit allowable under subsection (a)(1) for such taxable year, and

(B) The amounts which, by reason of this subsection, are added to the amount allowable for such taxable year and attributable to taxable years preceding the unused credit year.

(3) Effect of net operating loss carryback. To the extent that the excess described in paragraph (1) arises by reason of a net operating loss carryback, subparagraph (A) of paragraph (1) shall not apply.

(4) Taxable year beginning before January 1, 1962. For purposes of determining the amount of an investment credit carryback that may be added under paragraph (1) for a taxable year beginning before January 1, 1962, and ending after December 31, 1961, the amount of the limitation provided by subsection (a)(2) is the amount which bears the same ratio to such limitation as the number of days in such year after December 31, 1961, bears to the total number of days in such year.

(c) Qualified investment—(1) In general. For purposes of this subpart, the term "qualified investment" means, with respect to any taxable year, the aggregate of—

(A) The applicable percentage of the basis of each new section 38 property (as defined in section 48(b)) placed in service by the taxpayer during such taxable year, plus

(B) The applicable percentage of the cost of each used section 38 property (as defined in section 48(c)(1)) placed in service by the taxpayer during such taxable year.

(2) Applicable percentage. For purposes of paragraph (1), the applicable percentage for any property shall be determined under the following table:

If the useful life is—	The applicable percentage is—
4 years or more but less than 6 years.....	33 1/3
6 years or more but less than 8 years.....	66 2/3
8 years or more.....	100

For purposes of this paragraph, the useful life of any property shall be determined as of the time such property is placed in service by the taxpayer.

(3) Public utility property. (A) In the case of section 38 property which is public utility property, the amount of the qualified investment shall be 3/4 of the amount determined under paragraph (1).

(B) For purposes of subparagraph (A), the term "public utility property" means property used predominantly in the trade or business of the furnishing or sale of—

(i) Electrical energy, water, or sewage disposal services,

(ii) Gas through a local distribution system,

(iii) Telephone service, or

(iv) Telegraph service by means of domestic telegraph operations (as defined in section 222(a)(5) of the Communications Act of 1934, as amended; 47 U.S.C., sec. 222 (a)(5)).

If the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.

(4) Certain replacement property. For purposes of paragraph (1), if section 38 prop-

erty is placed in service by the taxpayer to replace property which was—

- (A) Destroyed or damaged by fire, storm, shipwreck, or other casualty, or
(B) Stolen,

the basis of such section 38 property (in the case of new section 38 property), or the cost of such section 38 property (in the case of used section 38 property), which (but for this paragraph) would be taken into account under paragraph (1) shall be reduced by an amount equal to the amount received by the taxpayer as compensation, by insurance or otherwise, for the property so destroyed, damaged, or stolen, or to the adjusted basis of such property, whichever is the lesser. No reduction in basis or cost shall be made under the preceding sentence in any case in which the reduction in qualified investment attributable to the substitution required by section 47(a)(1) with respect to the property so destroyed, damaged, or stolen (determined without regard to section 47(a)(4)) is greater than the reduction described in the preceding sentence.

(d) *Limitations with respect to certain persons*—(1) *In general.* In the case of—

(A) An organization to which section 593 applies,

(B) A regulated investment company or a real estate investment trust subject to taxation under subchapter M (sec. 851 and following), and

(C) A cooperative organization described in section 1381(a),

the qualified investment and the \$25,000 amount specified under subparagraphs (A) and (B) of subsection (a)(2) shall equal such person's ratable share of such items.

(2) *Ratable share.* For purposes of paragraph (1), the ratable share of any person for any taxable year of the items described therein shall be—

(A) In the case of an organization referred to in paragraph (1)(A), 50 percent thereof,

(B) In the case of a regulated investment company or a real estate investment trust, the ratio (i) the numerator of which is its taxable income and (ii) the denominator of which is its taxable income computed without regard to the deduction for dividends paid provided by section 852(b)(2)(D) or 857(b)(2)(C), as the case may be, and

(C) In the case of a cooperative organization, the ratio (i) the numerator of which is its taxable income and (ii) the denominator of which is its taxable income increased by amounts to which section 1382 (b) or (c) applies and similar amounts the tax treatment of which is determined without regard to subchapter T (sec. 1381 and following).

For purposes of subparagraph (B) of the preceding sentence, the term "taxable income" means in the case of a regulated investment company its investment company taxable income (within the meaning of section 852(b)(2)), and in the case of a real estate investment trust its real estate investment trust taxable income (within the meaning of section 857(b)(2)).

[Sec. 46 as added by sec. 2(b), Rev. Act 1962 (76 Stat. 963); as amended by sec. 201(d)(4), Rev. Act 1964 (78 Stat. 32)]

§ 1.46-1 Determination of amount.

(a) *In general.* Except as otherwise provided in this section and in § 1.46-2, the amount of the credit allowed by section 38 for the taxable year is equal to 7 percent of the taxpayer's qualified investment for such year (as determined under section 46(c)). The amount equal to 7 percent of qualified investment shall be referred to in this section and §§ 1.46-2 through 1.48-7 as the "credit earned".

(b) *Limitation based on amount of tax.* Notwithstanding the amount of the credit earned for the taxable year, the credit allowed by section 38 for the taxable year is limited to—

(1) If the liability for tax (as defined in paragraph (c) of this section) is \$25,000 or less, the liability for tax; or

(2) If the liability for tax is more than \$25,000, the first \$25,000 of the liability for tax plus 25 percent of the liability for tax in excess of \$25,000.

However, such \$25,000 amount may be reduced in the case of certain married individuals filing separate returns (see paragraph (e) of this section); corporations which are members of an affiliated group (see paragraph (f) of this section); trusts and estates (see paragraph (c) of § 1.48-6); and organizations to which section 593 applies, regulated investment companies or real estate investment trusts subject to taxation under subchapter M, chapter 1 of the Code, and cooperative organizations described in section 1381(a) (see § 1.46-4). The excess of the credit earned for the taxable year over the limitation described in this paragraph for such taxable year is an unused credit which may be carried back or forward to other taxable years in accordance with § 1.46-2.

(c) *Liability for tax.* For the purpose of computing the limitation based on amount of tax, section 46(a)(3) defines the liability for tax as the income tax imposed for the taxable year by chapter 1 (including the 2-percent tax on consolidated taxable income imposed with respect to taxable years beginning before January 1, 1964, and the 6-percent additional tax imposed by section 1562(b) with respect to taxable years ending after December 31, 1963), reduced by the sum of the credits allowable under—

(1) Section 33 (relating to taxes of foreign countries and possessions of United States),

(2) Section 34 (relating to dividends received by individuals before January 1, 1965),

(3) Section 35 (relating to partially tax-exempt interest received by individuals), and

(4) Section 37 (relating to retirement income).

For purposes of this paragraph, the tax imposed by section 531 (relating to imposition of accumulated earnings tax) or by section 541 (relating to imposition of personal holding company tax) shall not be considered tax imposed by chapter 1. Thus, the liability for tax and the credit allowed by section 38 for the taxable year are determined before computing any tax imposed by section 531 or 541. In addition, any increase in tax resulting from the application of section 47 (relating to certain dispositions, etc., of section 38 property) shall not be treated as tax imposed by chapter 1 for purposes of computing the liability for tax. See section 47(c).

(d) *Example.* The application of paragraphs (a), (b), and (c) of this section may be illustrated by the following example:

Example. X Corporation's qualified investment for its taxable year ending December

31, 1963, is \$2,050,000. X's credit earned for the taxable year is \$143,500 (7 percent of \$2,050,000). X's income tax for such year, computed without regard to credits against tax or tax imposed by section 531 or 541, is \$190,000. Such amount includes \$5,000 resulting from the application of section 47. X is allowed under section 33 a foreign tax credit of \$50,000. X's liability for tax is computed as follows:

<i>Liability for tax</i>	
Income tax (including increase in tax under section 47, but before credits and section 531 or 541 tax).....	\$190,000
Less: Increase in tax resulting from application of section 47.....	\$5,000
Foreign tax credit.....	50,000
	55,000
Liability for tax.....	135,000

X's credit allowed by section 38 for the taxable year is \$52,500 (\$25,000 plus 25 percent of \$110,000). X has an unused credit for the taxable year of \$91,000 (\$143,500 less \$52,500) which it may carry back or over to other taxable years in accordance with § 1.46-2.

(e) *Married individuals.* If a separate return is filed by a husband or wife, the limitation based on amount of tax under paragraph (b) of this section shall be computed by substituting a \$12,500 amount for the \$25,000 amount in applying paragraph (b) (1) and (2) of this section. However, this reduction of the \$25,000 amount to \$12,500 applies only if the taxpayer's spouse is entitled to a credit under section 38 for the taxable year of such spouse which ends with, or within, the taxpayer's taxable year. The taxpayer's spouse is entitled to a credit under section 38 either because of investment made in qualified property for such taxable year of the spouse (whether directly made by such spouse or whether apportioned to such spouse, for example, from an electing small business corporation, as defined in section 1371(b)), or because of an investment credit carryback or carryover to such taxable year. The determination of whether an individual is married shall be made under the principles of section 143 and the regulations thereunder.

(f) *Apportionment of \$25,000 amount among members of an affiliated group*—(1) *In general.* Section 46(a)(5) provides that in the case of an affiliated group (as defined in subparagraph (5) of this paragraph), the \$25,000 amount specified in section 46(a)(2) shall be reduced for each member of the group by apportioning \$25,000 among the members of the group. Except as otherwise provided in this paragraph, the \$25,000 amount shall be apportioned among those corporations which are members of the affiliated group on the last day of the taxable year of the common parent. For the taxable year of each such member ending with, or within which falls, the last day of the taxable year of the common parent, the credit allowed by section 38 cannot exceed—

(i) So much of its liability for tax for such taxable year as does not exceed its share of the \$25,000 amount apportioned to it under the rules prescribed in this paragraph, plus

(ii) 25 percent of so much of its liability for tax for such taxable year as

exceeds its share of the \$25,000 amount so apportioned to it.

(2) *Manner of apportionment.* (i) In the case of corporations which are members of an affiliated group on the last day of the taxable year of the common parent, the \$25,000 amount may be apportioned among such members (for the taxable year of each such member ending with, or within which falls, the last day of the taxable year of the common parent) in any manner the common parent may select, provided that the common parent, and each such member of the group less than 100 percent of the stock of which is owned in the aggregate by other members of the group on such last day, consent to the apportionment plan. However, no portion of the \$25,000 amount shall be apportioned to a taxable year ending before January 1, 1962. The consent of each member for which a consent is required to the apportionment plan shall be in the form of a statement signed by the member consenting to the plan. The statement shall set forth the name, address, and taxpayer account number of each member of the affiliated group on such last day (including those members in which other members own 100 percent of the stock) and of any other corporation to which any portion of such group's \$25,000 amount is apportionable under subparagraph (3) of this paragraph; the identity of the common parent; the last day of the common parent's taxable year; and the amount apportioned to each corporation. The consents may be incorporated in one statement. The statement (or statements) shall be attached to the timely filed income tax return of the common parent and shall be irrevocable after the due date of such return (including extensions of time). However, if the due date (including extensions of time) of the return of a common parent is before July 15, 1964, the required statement (or statements) shall be considered timely filed if filed on or before July 15, 1964, with the district director with whom the common parent files its return. Each member of the affiliated group on the last day of the taxable year of the common parent shall keep as a part of its records a copy of the consent of the common parent (or a copy of the statement containing all the required consents).

(ii) An apportionment plan adopted by an affiliated group with respect to a particular taxable year of the common parent shall be valid only for the taxable year of each member of the group which ends with, or within which falls, the last day of such taxable year of the common parent. Thus, an affiliated group must file a separate consent to an apportionment plan with respect to each taxable year of the common parent as to which an apportionment plan is desired.

(iii) If the apportionment plan is not timely selected, the \$25,000 amount specified in section 46(a)(2) shall be reduced for each member of the affiliated group, for its taxable year ending with, or within which falls, the last day of the common parent's taxable year, to an amount equal to (a) \$25,000, divided by (b) the number of corporations in such

group as of the close of such last day. If the taxable year of the common parent or any other member of such group ends before January 1, 1962, any such parent or member shall not be considered a member of the group for any such taxable year in determining the number of corporations referred to in (b) of the preceding sentence.

(iv) If a member of the affiliated group (including the common parent) makes its income tax return on the basis of a 52-53-week taxable year, the principles of section 441(f)(2)(A)(ii) and paragraph (b)(1) of § 1.441-2 apply in determining the last day of such a taxable year.

(3) *Short taxable year.* (i) If (a) the return of a corporation is for a short period ending after December 31, 1961, (b) such corporation is a member of an affiliated group as of the last day of such period, and (c) the last day of the common parent's taxable year does not end with or within such short period, then the \$25,000 amount shall be reduced for such corporation to an amount equal to \$25,000 divided by the number of corporations in such group as of the close of such corporation's short period. In such case, the total amount that may be apportioned under subparagraph (2) of this paragraph (either equally or according to a plan) among the members of an affiliated group which have the same common parent as the corporation with the short period shall be \$25,000 less the amount apportioned to such corporation for its short period ending in the taxable year of the common parent of the affiliated group. If the common parent of the corporation with the short period is not affiliated with any other corporation at the end of such parent's taxable year within which the short period ends, the \$25,000 amount shall be reduced for the parent by the amount apportioned to such corporation for its short period.

(ii) In lieu of the apportionment provided for in subdivision (i) of this subparagraph, a corporation (with a short period) may waive its right to receive the part of the \$25,000 amount apportionable to it by specifically so indicating on a statement meeting the requirements of subdivision (iii) of this subparagraph. In such case, no amount shall be considered apportioned to such corporation.

(iii) The corporation with the short period shall attach a statement to its timely filed income tax return (including extensions of time). However, if the due date of the return (including extensions of time) is before July 15, 1964, the statement may be filed on or before such date with the district director with whom the return has been filed. The statement shall indicate the name, address, and taxpayer account number of each member of the affiliated group as of the close of the short period; the identity of the common parent and the last day of the common parent's taxable year; and the amount apportioned to itself or, if appropriate, a waiver of the amount apportionable to it. A copy of the statement shall be furnished to the common parent.

(4) *Two or more common parents.* If a corporation during its taxable year

is a member of two or more affiliated groups as of the last day of the taxable year of the common parent of each such group, such corporation shall be considered to be a member of only the affiliated group whose common parent's taxable year ends earliest in such corporation's taxable year.

(5) *Definition of affiliated group.* For purposes of this paragraph, an affiliated group means one described in section 1504(a), except that all corporations shall be treated as includible corporations, without any exclusion under section 1504(b). Thus, a foreign corporation or a corporation exempt from taxation under section 501 may be a member of an affiliated group for purposes of this paragraph even though under section 1504(b) neither corporation would be an includible corporation.

(6) *Affiliated group filing a consolidated return.* The limitation based on amount of tax for an affiliated group all of whose members join in the filing of a consolidated return shall be so much of the consolidated liability for tax as does not exceed \$25,000, plus 25 percent of the consolidated liability for tax in excess of \$25,000. If, however, there are other members of the affiliated group which do not join in the filing of the consolidated return (such as a corporation exempt from taxation under section 501), and a consent is not timely filed apportioning the \$25,000 amount among the group filing the consolidated return and the other members of the affiliated group, each member of the affiliated group (including each member which joins in filing the consolidated return) shall be treated as a separate corporation for purposes of equally apportioning the \$25,000 amount under subparagraph (2)(iii) of this paragraph. In such case, the limitation based on amount of tax for the group filing the consolidated return shall be computed by substituting for the \$25,000 amount the total of the amounts apportioned to each corporation which joins in filing the consolidated return. If the group filing the consolidated return and the other members of the affiliated group adopt an apportionment plan, the group filing the consolidated return shall be treated as a single member for the purpose of applying subparagraph (2)(i) of this paragraph. Thus, for example, only one consent, executed by the common parent, to the apportionment plan is required for the group filing the consolidated return. If any member of the affiliated group which joins in the filing of the consolidated return is an organization to which section 593 applies or a cooperative organization described in section 1381(a), see paragraph (a)(2)(ii) of § 1.1502-51.

(7) *Nonresident foreign corporation.* (i) No part of the \$25,000 amount shall be apportioned under this paragraph to a foreign corporation not engaged in trade or business within the United States (hereinafter referred to in this subparagraph as a "nonresident foreign corporation"), nor shall such corporation be considered as a member for purposes of determining the number of corporations which divide equally the \$25,000 amount under subparagraph

(2)(iii) of this paragraph. Furthermore, the consent of such corporation to an apportionment plan is not required.

(ii) A nonresident foreign corporation which is a common parent of an affiliated group shall be considered to have a taxable year ending December 31.

(iii) If a nonresident foreign corporation is a common parent of an affiliated group, the statement (or statements) containing the consents of members of the group, required by subparagraph (2)(i) of this paragraph, shall be considered timely filed if filed with the Director, International Operations Division, Internal Revenue Service, Washington, D.C., 20225, on or before the 75th day after the end of its taxable year (as determined under subdivision (ii) of this subparagraph) or July 15, 1964, whichever is later.

(8) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

Example (1). P, a domestic corporation, files an income tax return for its taxable year ending January 31, 1962. On such date P owns all the outstanding stock of S, also a domestic corporation. S files a separate income tax return on the basis of a fiscal year ending June 30. The membership of the affiliated group is ascertained as of the close of January 31, 1962, the last day of the taxable year of the common parent, P. On that day the affiliated group consists of P and S. P consents to an apportionment plan in which the \$25,000 amount is apportioned entirely to S for its taxable year ending June 30, 1962 (S's taxable year within which the last day of the taxable year of the common parent, January 31, 1962, falls). Such consent is timely filed. For purposes of computing the credit under section 38, S's limitation based on amount of tax for its taxable year ending June 30, 1962, is so much of S's liability for tax as does not exceed \$25,000, plus 25 percent of S's liability for tax in excess of \$25,000. P's limitation for its taxable year ending January 31, 1962, is equal to 25 percent of P's liability for tax. On the other hand, if an apportionment plan is not timely filed, P's limitation would be so much of P's liability for tax as does not exceed \$12,500 plus 25 percent of P's liability for tax in excess of \$12,500, and S's limitation would be computed similarly.

Example (2). Assume the same facts as in example (1), except that P's taxable year ends December 31, 1961, on which date it owns all the outstanding stock of S. No portion of the \$25,000 amount is apportioned to P since its taxable year ends before January 1, 1962. Accordingly, S is apportioned the entire \$25,000 amount for its taxable year ending June 30, 1962.

Example (3). F, a domestic corporation exempt from taxation under section 501, files a return for its taxable year ending December 31, 1963, on which date it owns all the stock of P, a domestic corporation. P files a consolidated return as a common parent for its fiscal year ending June 30, 1964, with its two wholly owned domestic subsidiaries, S and A. The membership of the affiliated group is ascertained as of the close of December 31, 1963, the last day of the taxable year of the common parent, F, and accordingly consists of F, P, S, and A. No consent to an apportionment plan is filed. Therefore, each member is apportioned \$6,250 of the \$25,000 amount (\$25,000 divided by the four members). The limitation based on amount of tax for the affiliated group filing a consolidated return (P, S, and A) for the year ending June 30, 1964 (the consolidated taxable year within which December 31, 1963, falls), is computed by using \$18,750

instead of the \$25,000 amount. The \$18,750 is arrived at by adding together the \$6,250 amounts apportioned to P, S, and A. If the consolidated liability for tax of P, S, and A is \$27,750 for the taxable year ending June 30, 1964, then the credit allowed by section 38 for such group for such taxable year cannot exceed \$21,000 (\$18,750 plus 25 percent of \$9,000).

Example (4). Assume the same facts as in example (3), except that a consent by F is filed with the timely filed return of F apportioning the entire \$25,000 amount to the group filing a consolidated tax return (P, S, and A). The credit allowed by section 38 for such group for its taxable year ending June 30, 1964, cannot exceed \$25,687.50 (\$25,000 plus 25 percent of \$2,750).

Example (5). P, a domestic corporation filing income tax returns on a calendar-year basis, owns all the stock of S, T, and U, all domestic corporations. S, T, and U file separate returns on a calendar-year basis. On June 30, 1963, S is liquidated, and therefore has a short taxable year beginning January 1, 1963, and ending June 30, 1963. S does not waive its right to its equal portion of the \$25,000 amount. For such short taxable year, the \$25,000 amount shall be reduced for S to \$6,250 (\$25,000 divided by 4, the number of corporations in the affiliated group at the close of S's short taxable year). The total amount apportionable to the members of the affiliated group of which P is the common parent for their taxable years ending December 31, 1963, is \$18,750 (\$25,000 minus the \$6,250 apportioned to S for its short taxable year ending June 30, 1963). The \$18,750 amount may be apportioned according to an apportionment plan or, if a plan is not timely filed, will be apportioned equally among P, T, and U.

§ 1.46-2 Carryback and carryover of unused credit.

(a) *Allowance of unused credit as carryback or carryover.* (1) Section 46

(b)(1) provides for a 3-year carryback and a 5-year carryover of any unused credit. An unused credit is the excess of the credit earned for the taxable year (as defined in paragraph (a) of § 1.46-1) over the limitation based on amount of tax for such taxable year (as determined under paragraph (b) of § 1.46-1). Subject to the limitation contained in paragraph (b) of this section, an unused credit shall be added to the amount allowable as a credit under section 38 for the years to which the unused credit can be carried. The year with respect to which an unused credit arises shall be referred to in this section as the "unused credit year".

(2) An unused credit shall be an investment credit carryback to each of the 3 taxable years preceding the unused credit year and an investment credit carryover to each of the 5 taxable years succeeding the unused credit year, except that an unused credit shall be a carryback only to taxable years ending after December 31, 1961. An unused credit must be carried first to the earliest of the 8 taxable years to which it may be carried, and then to each of the other 7 taxable years (in order of time) to the extent that the unused credit may not be added (because of the limitation contained in paragraph (b) of this section) to the amount allowable as a credit under section 38 for a prior taxable year.

(b) *Limitation on allowance of unused credit.* The amount of the unused credit from any particular unused credit year which may be added to the amount

allowable as a credit under section 38 for any of the 3 preceding or 5 succeeding taxable years to which such credit may be carried shall not exceed the amount by which the limitation based on amount of tax for such preceding or succeeding taxable year exceeds the sum of (1) the credit earned for such preceding or succeeding year, and (2) other unused credits carried to such preceding or succeeding year which are attributable to unused credit years prior to the particular unused credit year. Thus, in determining the amount, if any, of an unused credit from a particular unused credit year which shall be added to the amount allowable as a credit for any preceding or succeeding taxable year, the credit earned for such preceding or succeeding taxable year, plus any unused credits originating in taxable years prior to the particular unused credit year, shall first be applied against the limitation based on amount of tax for such preceding or succeeding taxable year. To the extent the limitation based on amount of tax for the preceding or succeeding year exceeds the sum of the credit earned for such year and other unused credits attributable to years prior to the particular unused credit year, the unused credit from the particular unused credit year shall be added to the amount allowable as a credit under section 38 for such preceding or succeeding year. To the extent that an unused credit cannot be added for a particular preceding or succeeding taxable year because of the limitation contained in this paragraph, such unused credit shall be available as a carryback or carryover to the next succeeding taxable year to which it may be carried.

(c) *Effect of net operating loss carryback.* If the effect of a net operating loss carryback is to create an unused credit (as defined in paragraph (a) (1) of this section), such unused credit shall not be treated as an investment credit carryback. However, the full amount of the unused credit so arising shall be available for use as an investment credit carryover for the 5 taxable years following the unused credit year. Thus, assume a taxpayer's credit earned for its taxable year 1965 is \$25,000, and such credit is allowable in full under section 38 for such year. In a subsequent taxable year, such taxpayer has a net operating loss which he carries back to 1965 and which results in eliminating the taxpayer's taxable income and liability for tax for 1965. In such case, the \$25,000 credit earned (no longer allowable for the year 1965) becomes an unused credit which, although it shall not be treated as an investment credit carryback, shall be carried forward to 1966 and to each of the subsequent years to which it may be carried.

(d) *Taxable years beginning before January 1, 1962, and ending after December 31, 1961.* Section 46(b)(4) provides a transition rule relating to the amount of an investment credit carryback which may be added to the amount allowable as a credit under section 38 for a taxable year beginning before January 1, 1962, and ending after December 31, 1961. For purposes of determining

the amount of unused credits which may be carried back to such a taxable year and added to the amount allowable as a credit for such year, the limitation based on amount of tax for such year (determined without regard to this paragraph) shall be reduced to an amount which bears the same ratio to such limitation as the number of days in such taxable year after December 31, 1961, bears to the total number of days in such year.

(e) *Corporate acquisitions.* For the carryover of unused credits in the case of certain corporate acquisitions, see section 381(c) (23).

(f) *Periods of less than 12 months.* A fractional part of a year which is considered as a taxable year under sections 441(b) and 7701(a) (23) shall be treated as a preceding or a succeeding taxable year for the purpose of determining under section 46(b) the taxable years to which an unused credit may be carried.

(g) *Examples.* The provisions of paragraphs (a) through (f) of this section may be illustrated by the following examples:

Example (1). Corporation X files its income tax return on the basis of the calendar year. X's credit earned and its limitation based on amount of tax for each of its taxable years 1962 through 1968 are as follows:

	Credit earned	Limitation based on amount of tax
1962	\$175,000	\$200,000
1963	250,000	190,000
1964	200,000	210,000
1965	210,000	230,000
1966	220,000	260,000
1967	260,000	220,000
1968	270,000	280,000

(1) Corporation X's credit earned for 1962, \$175,000, is allowable in full as a credit under section 38 for 1962 since such amount is less than the limitation based on amount of tax for such year, \$200,000. Since the limitation based on amount of tax for 1963 is \$190,000, only \$160,000 of the \$250,000 credit earned for such year is allowable under section 38 as a credit for 1963. The unused credit for 1963 of \$90,000 (\$250,000 less \$160,000) is an investment credit carryback to 1962 and an investment credit carryover to 1964 and subsequent years. The portions of the \$90,000 unused credit which shall be added to the amount allowable as a credit under section 38 for 1962 and for 1964 and subsequent years are computed as follows:

(a) 1962. The portion of the unused credit for 1963 (\$90,000) which is allowable as a credit for 1962 is \$25,000. This amount shall be added to the amount allowable as a credit for 1962. The balance of the unused credit for 1963 to be carried to 1964 is \$65,000. These amounts are computed as follows:

Carryback to 1962	\$90,000
1962 limitation based on tax	\$200,000
Less: Credit earned for 1962	\$175,000
Unused credits attributable to years preceding 1963	0
Limit on amount of 1963 unused credit which may be added as a credit for 1962	25,000
Balance of 1963 unused credit to be carried to 1964	65,000

(b) 1964. The portion of the balance of the unused credit for 1963 (\$65,000) allowable as a credit for 1964 is \$10,000. This amount shall be added to the amount allowable as a credit for 1964. The balance of the unused credit for 1963 to be carried to 1965

is \$55,000. These amounts are computed as follows:

Carryover to 1964	\$65,000
1964 limitation based on tax	\$210,000
Less: Credit earned for 1964	\$200,000
Unused credits attributable to years preceding 1963	0
Limit on amount of 1963 unused credit which may be added as a credit for 1964	10,000
Balance of 1963 unused credit to be carried to 1965	55,000

(c) 1965. The portion of the balance of the unused credit for 1963 (\$55,000) allowable as a credit for 1965 is \$20,000. This amount shall be added to the amount allowable as a credit for 1965. The balance of the unused credit for 1963 to be carried to 1966 is \$35,000. These amounts are computed as follows:

Carryover to 1965	\$55,000
1965 limitation based on tax	\$230,000
Less: Credit earned for 1965	\$210,000
Unused credits attributable to years preceding 1963	0
Limit on amount of 1963 unused credit which may be added as a credit for 1965	20,000
Balance of 1963 unused credit to be carried to 1966	35,000

(d) 1966. The entire balance of the unused credit for 1963 (\$35,000) is allowable as a credit for 1966, since the limitation based on amount of tax for 1966 exceeds the sum of the credit earned for 1966 and unused credits attributable to years prior to 1963 by an amount in excess of \$35,000. Since the balance of the unused credit for 1963 has been fully allowed, no portion thereof remains to be carried to 1967 or 1968. This is illustrated as follows:

Carryover to 1966	\$35,000
1966 limitation based on tax	\$260,000
Less: Credit earned for 1966	\$220,000
Unused credits attributable to years preceding 1963	0
Limit on amount of 1963 unused credit which may be added as a credit for 1966	40,000
Balance of 1963 unused credit to be carried to 1967	0

(ii) Since the limitation based on amount of tax for 1967 is \$220,000, only \$220,000 of the \$260,000 credit earned for such year is allowable as a credit for 1967. The unused credit for 1967 of \$40,000 (\$260,000 less \$220,000) is an investment credit carryback to 1964, 1965, and 1966 and an investment credit carryover to 1968 and subsequent years. The portions of the \$40,000 unused credit which shall be added to the amount allowable as a credit for such years are computed as follows:

(a) 1964. The portion of the unused credit for 1967 (\$40,000) allowable as a credit for 1964 is zero. The balance of the unused credit for 1967 to be carried to 1965 is \$40,000. These amounts are computed as follows:

Carryback to 1964	\$40,000
1964 limitation based on tax	\$210,000
Less: Credit earned for 1964	\$200,000
Unused credits attributable to years preceding 1967 (unused credit from 1963)	10,000
Limit on amount 1967 unused credit which may be added as a credit for 1964	0
Balance of 1967 unused credit to be carried to 1965	40,000

(b) 1965. The portion of the unused credit for 1967 (\$40,000) allowable as a credit for 1965 is zero. The balance of the unused credit for 1967 to be carried to 1966

is \$40,000. These amounts are computed as follows:

Carryback to 1965	\$40,000
1965 limitation based on tax	\$230,000
Less: Credit earned for 1965	\$210,000
Unused credits attributable to years preceding 1967 (unused credit from 1963)	20,000
Limit on amount of 1967 unused credit which may be added as a credit for 1965	0
Balance of 1967 unused credit to be carried to 1966	40,000

(c) 1966. The portion of the unused credit for 1967 (\$40,000) allowable as a credit for 1966 is \$5,000. This amount shall be added to the amount allowable as a credit for 1966. The balance of the unused credit for 1967 to be carried to 1968 is \$35,000. These amounts are computed as follows:

Carryback to 1966	\$40,000
1966 limitation based on tax	\$260,000
Less: Credit earned for 1966	\$220,000
Unused credits attributable to years preceding 1967 (unused credit from 1963)	35,000
Limit on amount of 1967 unused credit which may be added as a credit for 1966	5,000
Balance of 1967 unused credit to be carried to 1968	35,000

(d) 1968. The portion of the balance of the unused credit for 1967 (\$35,000) allowable as a credit for 1968 is \$10,000. This amount shall be added to the amount allowable as a credit for 1968. The balance of the unused credit for 1967 to be carried to 1969 and subsequent years is \$25,000. These amounts are computed as follows:

Carryover to 1968	\$35,000
1968 limitation based on tax	\$280,000
Less: Credit earned for 1968	\$270,000
Unused credits attributable to years preceding 1967	0
Limit on amount of 1967 unused credit which may be added as a credit for 1968	10,000
Balance of 1967 unused credit to be carried to 1969	25,000

Example (2). Corporation Y files its income tax return on the basis of a fiscal year ending June 30. For its taxable year beginning July 1, 1961, and ending June 30, 1962, Y's credit earned is \$65,000, and its limitation based on amount of tax is \$200,000. The full credit earned (\$65,000) is allowable for Y's taxable year ending June 30, 1962, as a credit against tax since such amount is less than the limitation (\$200,000). For purposes of determining the amount of an investment credit carryback from any subsequent taxable year which may be added to the amount allowable as a credit for the taxable year ending June 30, 1962, the limitation based on amount of tax for such year shall be reduced from \$200,000 to \$99,178 ($200,000 \times 181/365$). Therefore, the total investment credit carrybacks to the taxable year ending June 30, 1962, may not exceed \$34,178 (\$99,178 less \$65,000).

(h) *Electing small business corporation.* An unused credit of a corporation which arises in an unused credit year for which the corporation is not an electing small business corporation (as defined in section 1371(b)) and which is a carryback or carryover to a taxable year for which the corporation is an electing small business corporation shall not be added to the amount allowable as a credit under section 38 to the shareholders of such corporation for any taxable year. However, a taxable year for which the corporation is an electing small business

corporation shall be counted as a taxable year for purposes of determining the taxable years to which such unused credit may be carried.

§ 1.46-3 Qualified investment.

(a) *In general.* (1) With respect to any taxable year, the qualified investment of the taxpayer is the aggregate (expressed in dollars) of (i) the applicable percentage of the basis of each new section 38 property placed in service by the taxpayer during such taxable year, plus (ii) the applicable percentage of the cost of each used section 38 property placed in service by the taxpayer during such taxable year. With respect to any section 38 property, qualified investment means the applicable percentage of the basis (or cost) of such property. Section 38 property placed in service by the taxpayer during the taxable year includes the taxpayer's share of the basis (or cost) of section 38 property placed in service by a partnership in the taxable year of such partnership ending with or within the taxpayer's taxable year. In the case of a shareholder of an electing small business corporation (as defined in section 1371(b)), or a beneficiary of an estate or trust, see §§ 1.48-5 and 1.48-6, respectively, for apportionment of the basis (or cost) of section 38 property placed in service by such corporation, estate, or trust. For the definitions of new section 38 property and used section 38 property, see §§ 1.48-2 and 1.48-3, respectively.

(2) The basis (or cost) of section 38 property placed in service during a taxable year shall not be taken into account in determining qualified investment for such year if such property is disposed of or otherwise ceases to be section 38 property during such year, except where section 47(b) or 46(c)(4) applies. Thus, if individual A places in service during a taxable year section 38 property and later in the same year sells such property, the basis (or cost) of such property shall not be taken into account in determining A's qualified investment. On the other hand, if A places in service section 38 property during a taxable year and dies later in the same year, the basis (or cost) of such property would be taken into account in computing qualified investment. Similarly, if section 38 property is destroyed by fire in the same year in which it is placed in service and section 46(c)(4) applies to reduce the basis (or cost) of replacement property, the basis (or cost) of the destroyed property would be taken into account in computing qualified investment.

(3) Qualified investment is reduced in the case of property which is "public utility property" (see paragraph (h) of this section), and in the case of property of organizations to which section 593 applies, regulated investment companies or real estate investment trusts subject to taxation under subchapter M, chapter 1 of the Code, and cooperative organizations described in section 1381(a) (see § 1.46-4).

(b) *Applicable percentage.* The applicable percentage to be applied to the basis (or cost) of property is 33 1/3 percent if the estimated useful life of the

property is 4 years or more but less than 6 years; 66 2/3 percent if the estimated useful life is 6 years or more but less than 8 years; or 100 percent if the estimated useful life is 8 years or more. The provisions of this paragraph may be illustrated by the following example:

Example. Corporation Y acquires and places in service during 1963 the following new and used section 38 properties:

Property	Estimated useful life	Basis (or cost)
A (new).....	5 years.....	\$80,000
B (new).....	10 years.....	90,000
C (new).....	6 years.....	150,000
D (used).....	4 years.....	30,000

Corporation Y's qualified investment for 1963 is \$220,000 determined in the following manner:

Property	Basis (or cost)	Applicable percentage	Qualified investment
A.....	\$80,000	33 1/3	\$20,000
B.....	90,000	100	90,000
C.....	150,000	66 2/3	100,000
D.....	30,000	33 1/3	10,000
Total.....			220,000

(c) *Basis or cost.* (1) The basis of any new section 38 property shall be determined in accordance with the general rules for determining the basis of property. Thus, the basis of property would generally be its cost (see section 1012), unreduced by the adjustment to basis provided by section 48(g)(1) with respect to property placed in service before January 1, 1964, and any other adjustment to basis, such as that for depreciation, and would include all items properly included by the taxpayer in the depreciable basis of the property, such as installation and freight costs. However, for purposes of determining qualified investment, the basis of new section 38 property constructed, reconstructed, or erected by the taxpayer shall not include any depreciation sustained with respect to any other property used in the construction, reconstruction, or erection of such new section 38 property. (See paragraph (b)(4), of § 1.48-1.)

If new section 38 property is acquired in exchange for cash and other property in a transaction described in section 1031 in which no gain or loss is recognized, the basis of the newly acquired property for purposes of determining qualified investment would be equal to the adjusted basis of the other property plus the cash paid. See § 1.48-4 for the basis of property to a lessee where the lessor has elected to treat such lessee as a purchaser.

(2) The cost of any used section 38 property shall be determined in accordance with paragraph (b) of § 1.48-3. However, the aggregate cost of used section 38 property which may be taken into account in any taxable year in computing qualified investment cannot exceed \$50,000 (see paragraph (c) of § 1.48-3).

(3) For reduction in the basis (or cost) of certain property which replaces other property which was destroyed or damaged by fire, storm, shipwreck, or

other casualty, or which was stolen, see section 46(c)(4).

(d) *Placed in service.* (1) For purposes of the credit allowed by section 38, property shall be considered placed in service in the earlier of the following taxable years:

(i) The taxable year in which, under the taxpayer's depreciation practice, the period for depreciation with respect to such property begins; or

(ii) The taxable year in which the property is placed in a condition or state of readiness and availability for a specifically assigned function, whether in a trade or business, in the production of income, in a tax-exempt activity, or in a personal activity.

Thus, if property meets the conditions of subdivision (ii) of this subparagraph in a taxable year, it shall be considered placed in service in such year notwithstanding that the period for depreciation with respect to such property begins in a succeeding taxable year because, for example, under the taxpayer's depreciation practice such property is accounted for in a multiple asset account and depreciation is computed under an "averaging convention" (see § 1.167(a)-10), or depreciation with respect to such property is computed under the completed contract method, the unit of production method, or the retirement method.

(2) In the case of property acquired by a taxpayer for use in his trade or business (or in the production of income), the following are examples of cases where property shall be considered in a condition or state of readiness and availability for a specifically assigned function:

(i) Parts are acquired and set aside during the taxable year for use as replacements for a particular machine (or machines) in order to avoid operational time loss.

(ii) Operational farm equipment is acquired during the taxable year and it is not practicable to use such equipment for its specifically assigned function in the taxpayer's business of farming until the following year.

(iii) Equipment is acquired for a specifically assigned function and is operational but is undergoing testing to eliminate any defects. However, fruit-bearing trees and vines shall not be considered in a condition or state of readiness and availability for a specifically assigned function until they have reached an income-producing stage. Moreover, materials and parts acquired to be used in the construction of an item of equipment shall not be considered in a condition or state of readiness and availability for a specifically assigned function.

(3) Notwithstanding subparagraph (1) of this paragraph, property with respect to which an election is made under § 1.48-4 to treat the lessee as having purchased such property shall be considered placed in service by the lessor in the taxable year in which possession is transferred to such lessee.

(4) (i) The credit allowed by section 38 with respect to any property shall be allowed only for the first taxable year

in which such property is placed in service by the taxpayer. The determination of whether property is section 38 property in the hands of the taxpayer shall be made with respect to such first taxable year. Thus, if a taxpayer places property in service in a taxable year and such property does not qualify as section 38 property (or only a portion of such property qualifies as section 38 property) in such year, no credit (or a credit only as to the portion which qualifies in such year) shall be allowed to the taxpayer with respect to such property notwithstanding that such property (or a greater portion of such property) qualifies as section 38 property in a subsequent taxable year. For example, if a taxpayer places property in service in 1963 and uses the property entirely for personal purposes in such year, but in 1964 begins using the property in a trade or business, no credit is allowable to the taxpayer under section 38 with respect to such property. See § 1.48-1 for the definition of section 38 property.

(ii) Notwithstanding subdivision (i) of this subparagraph, if, for the first taxable year in which property is placed in service by the taxpayer, the property qualifies as section 38 property but the basis of the property does not reflect its full cost for the reason that the total amount to be paid or incurred by the taxpayer for the property is indeterminate, a credit shall be allowed to the taxpayer for such first taxable year with respect to so much of the cost as is reflected in the basis of the property as of the close of such year, and an additional credit shall be allowed to the taxpayer for any subsequent taxable year with respect to the additional cost paid or incurred during such year and reflected in the basis of the property as of the close of such year. The estimated useful life used in computing each additional credit with respect to the property shall be the same as the estimated useful life used in computing the credit for the first taxable year in which the property was placed in service by the taxpayer. Assume, for example, that in 1964 X Corporation, a utility company which makes its return on the basis of a calendar year, enters into an agreement with Y Corporation, a builder, to construct certain utility facilities for a housing development built by Y. Assume further that part of the funds for the construction of the utility facilities is advanced by Y under a contract providing that X will repay the advances over a 10-year period in accordance with an agreed formula, after which no further amounts will be repayable by X even though the full amount advanced by Y has not been repaid. Assuming that the utility facilities are placed in service in 1964 and qualify as section 38 property, X is allowed a credit for 1964 with respect to its basis in the utility facilities at the close of 1964. For each succeeding taxable year X is allowed an additional credit with respect to the increase in the basis of the utility facilities resulting from the repayments to Y during such year.

(e) *Estimated useful life*—(1) *In general*. With respect to assets placed in

service by the taxpayer during any taxable year, for the purpose of computing qualified investment the estimated useful lives assigned to all assets which fall within a particular guideline class (within the meaning of Revenue Procedure 62-21) may be determined, at the taxpayer's option, under either subparagraph (2) or (3) of this paragraph. Thus, the taxpayer may assign estimated useful lives to all the assets falling in one guideline class in accordance with subparagraph (2) of this paragraph, and may assign estimated useful lives to all the assets falling within another guideline class in accordance with subparagraph (3) of this paragraph. See subparagraphs (4) and (5) of this paragraph for determination of estimated useful lives of assets not subject to subparagraph (2) or (3) of this paragraph.

(2) *Class life system*. The taxpayer may assign to each asset falling within a guideline class, which is placed in service during the taxable year, the class life of the taxpayer for the guideline class for such year as determined under section 4, Part II of Revenue Procedure 62-21. The preceding sentence may be applied to the assets falling within a guideline class irrespective of whether the taxpayer uses single asset accounts or multiple asset accounts in computing depreciation with respect to such assets and irrespective of whether the taxpayer chooses to have his depreciation allowance with respect to such assets examined under the rules provided in Revenue Procedure 62-21.

(3) *Individual useful life system*. (1) The taxpayer may assign an individual estimated useful life to each asset falling within a guideline class which is placed in service during the taxable year. With respect to the assets falling within the guideline class which are placed in single asset accounts for purposes of computing depreciation, the estimated useful life used for each asset for that purpose shall be used in determining qualified investment. With respect to the assets falling within the guideline class which are placed in multiple asset accounts (including a guideline class account described in Revenue Procedure 62-21) for which a group, classified, or composite rate is used in computing depreciation (or in single asset accounts for which an average life rate is used), the determination of estimated useful life for each asset in the account shall be made individually on the best estimate obtainable on the basis of all the facts and circumstances. The individual estimated useful lives used for all the assets placed in a multiple asset account, when viewed together, must be consistent with the group, classified, or composite rate used for the account for purposes of computing depreciation.

(ii) In determining the individual estimated useful lives of assets similar in kind contained in a multiple asset account (or in single asset accounts for which an average life rate is used), the taxpayer may assign to each of such assets the average useful life of such assets used for purposes of computing

depreciation, or he may assign separate lives to such assets based on the estimated range of years taken into consideration in establishing the average useful life. Thus, for example, if a taxpayer places 9 similar trucks with an average estimated useful life of 7 years, based on an estimated range of 6 to 8 years (2 trucks with a useful life of 6 years, 5 trucks with a useful life of 7 years, and 2 trucks with a useful life of 8 years), in a multiple asset account for which a group rate is used in computing depreciation, he may either assign a useful life of 6 years to 2 of the trucks, 7 years to 5 of the trucks, and 8 years to 2 of the trucks, or he may assign the average useful life of the trucks (7 years) to each of the 9 trucks. Similarly, if a taxpayer places 100 telephone poles with an average useful life of 28 years, based on an estimated range of 3 to 40 years (2 with a useful life of less than 4 years, 3 with a useful life of 4 to 6 years, 4 with a useful life of 6 to 8 years, and 91 with a useful life of more than 8 years), in a multiple asset account for which a group rate is used in computing depreciation, he may either assign useful lives corresponding to the estimated range of years of the poles (i.e., a useful life of less than 4 years to 2 of the poles, etc.), or he may assign the average useful life of the poles (28 years) to each of the poles.

(4) *Useful life of property subject to amortization*. In the case of property with respect to which amortization in lieu of depreciation is allowable, the term over which amortization deductions are taken shall be considered as the estimated useful life of such property.

(5) *Useful life of property subject to certain methods of depreciation*. If a taxpayer is using a method of depreciation, such as the unit of production or retirement method, which does not measure the useful life of the property in terms of years, he must estimate such useful life in years in order to compute his qualified investment.

(6) *Record requirements*. The taxpayer shall maintain sufficient records to determine whether section 47 (relating to certain dispositions, etc., of section 38 property) applies with respect to any asset.

(f) *Partnerships*—(1) *In general*. In the case of a partnership, each partner shall take into account separately, for his taxable year with or within which the partnership taxable year ends, his share of the basis of partnership new section 38 property and his share of the cost of partnership used section 38 property placed in service by the partnership during such partnership taxable year. Each partner shall be treated as the taxpayer with respect to his share of the basis of partnership new section 38 property and his share of the cost of partnership used section 38 property. The estimated useful life to each partner of such property shall be deemed to be the estimated useful life of the property in the hands of the partnership. Partnership section 38 property shall not, by reason of each partner taking his share of the basis or cost into account, lose its character as either new section 38 prop-

erty or used section 38 property, as the case may be.

(2) *Determination of partner's share.*

(i) Each partner's share of the basis (or cost) of any section 38 property shall be determined in accordance with the ratio in which the partners divide the general profits of the partnership (that is, the taxable income of the partnership as described in section 702(a)(9)). However, if the ratio in which the partners divide the general profits of the partnership changes during the taxable year of the partnership, the ratio effective for the date on which the property is placed in service shall apply.

(ii) Notwithstanding subdivision (i) of this subparagraph, if all related items of income, gain, loss, and deduction with respect to any item of partnership section 38 property are specially allocated in the same manner and if such special allocation is recognized under section 704 (a) and (b) and paragraph (b) of § 1.704-1, then each partner's share of the basis of such item of new section 38 property or the cost of such item of used section 38 property shall be determined by reference to such special allocation effective for the date on which the property is placed in service.

(3) *Examples.* This paragraph may be illustrated by the following examples:

Example (1). Partnership ABCD acquires and places in service on January 1, 1962, an item of new section 38 property, and acquires and places in service on September 1, 1962, another item of new section 38 property. The ABCD partnership and each of its partners reports income on the basis of the calendar year. Partners A, B, C, and D share partnership profits equally. Each partner's share of the basis of each new partnership section 38 property is 25 percent.

Example (2). Assume the same facts as in example (1) and the following additional facts: A dies on June 30, 1962, and B purchases A's interest as of such date. Each partner's share of the profits from January 1 to June 30 is 25 percent. From July 1 to December 31, B's share of the profits is 50 percent, and C and D's share of the profits is 25 percent each. For A's last taxable year (January 1 to June 30, 1962), A shall take into account 25 percent of the basis of the section 38 property placed in service on January 1 and 50 percent of the basis of the section 38 property placed in service on September 1. C and D shall each take into account 25 percent of the basis of each new section 38 property placed in service by the partnership in 1962.

Example (3). Partnership MR is engaged in the business of renting soda fountain equipment and ice makers to restaurants. The partnership makes no elections under § 1.48-4 to treat its lessees as having purchased such property. Under the terms of the partnership agreement, the income, gain or loss on disposition, depreciation, and other deductions attributable to the ice makers are specially allocated 70 percent to partner M and 30 percent to partner R. In all other respects M and R share profits and losses equally. If the special allocation with respect to the ice makers is recognized under section 704 (a) and (b) and paragraph (b) of § 1.704-1, the basis (or cost) of the ice makers which qualify as partnership section 38 property shall be taken into account 70 percent by M and 30 percent by R. The basis (or cost) of partnership section 38 property not subject to the special

allocation shall be taken into account equally by M and R.

Example (4). Assume the same facts as in example (3) and the following additional facts: During November 1962, the partnership, which reports its income on the basis of a fiscal year ending May 31, acquires and places in service two items which qualify as new section 38 property, an icemaker and a soda fountain. The icemaker has an estimated useful life of 8 years to the partnership and a basis of \$1,000. The soda fountain has an estimated useful life of 6 years to the

partnership and a basis of \$600. Partner M also owns and operates a business as a sole proprietorship and reports income on the calendar year basis. During 1963, M acquires and places in service in his sole proprietorship a machine which qualifies as new section 38 property. This machine has an estimated useful life of 4 years and a basis of \$300. M owns no interest in any other partnerships, electing small business corporations, estates, or trusts. M's total qualified investment for 1963 is \$1,000, computed as follows:

Property	Estimated useful life	Basis	M's share of basis	Applicable percentage	Qualified investment
<i>Partnership MR</i>					
Icemaker	8	\$1,000	\$700	100	\$700
Soda fountain	6	600	300	66⅔	200
<i>Sole proprietorship</i>					
Machine	4	300		33⅓	100
Total					1,000

(g) *Public utility property.* (1) In the case of section 38 property which is public utility property, the amount of the qualified investment with respect to such property shall be ⅔ of the amount otherwise determined under this section with respect to such property.

(2) The term "public utility property" means property used predominantly in the trade or business of the furnishing or sale of—

(i) Electrical energy, water, or sewage disposal services,

(ii) Gas through a local distribution system,

(iii) Telephone service, or

(iv) Telegraph service by means of domestic telegraph operations (as defined in section 222(a)(5) of the Communications Act of 1934, as amended; 47 U.S.C., sec. 222(a)(5)).

If the rates for such furnishing or sale, as the case may be, have been established or approved by a State (including the District of Columbia) or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof. The term "established or approved" includes the filing of a schedule of rates with any body named in the preceding sentence which has the power to approve such rates, even though such body has taken no action on the filed schedule. For purposes of this paragraph, any activity described in subdivision (i), (ii), (iii), or (iv) of this subparagraph, which is regulated in a manner described in this subparagraph, shall be referred to as a "public utility activity". If property is used by a taxpayer both in a public utility activity and in another activity, the characterization of such property shall be based on the predominant use of such property during the taxable year in which it is placed in service.

(3) Public utility property includes property which is leased to others by a taxpayer where the leasing of such property is part of the lessor's public utility activity. Thus, such leased property is public utility property even though the lessee uses such property in

an activity which is not a public utility activity, and whether or not the lessor of such property makes a valid election under § 1.48-4 to treat the lessee as having purchased such property for purposes of the credit allowed by section 38. Property leased by a lessor, where the leasing is not part of a public utility activity, to a lessee who uses such property predominantly in a public utility activity is public utility property for purposes of computing the lessor's or lessee's qualified investment with respect to such property.

(4) (i) With respect to properties of a taxpayer engaged in both the production or transmission of gas and the local distribution of gas, section 38 property shall be considered as used predominantly in the trade or business of the furnishing or sale of gas through a local distribution system if expenditures for such property are chargeable to any of the following accounts under either the uniform system of accounts prescribed for natural gas companies (class A and class B) by the Federal Power Commission, effective January 1, 1961, or the uniform system of accounts for class A and B gas utilities adopted in 1958 by the National Association of Railroad and Utility Commissioners (or would be chargeable to any of the following accounts if the taxpayer used either of such systems):

(a) Accounts 360 through 363, inclusive (Local Storage Plant), or

(b) Accounts 374 through 387, inclusive (Distribution Plant).

(ii) If expenditures for section 38 property are chargeable (or would be chargeable) to any of the following accounts under either of the systems named in subdivision (i) of this subparagraph, the determination of whether or not such property is used predominantly in the trade or business of the furnishing or sale of gas through a local distribution system shall be made under all the facts and circumstances relating to the actual use of such property in the year such property is placed in service:

(a) Accounts 304 through 320, inclusive (Manufactured Gas Production Plant), or

(b) Accounts 389 through 399, inclusive (General Plant).

For example, if an office machine is used 55 percent of the time for billing customers of the taxpayer's local distribution system in the year in which it is placed in service, such office machine shall be considered as used predominantly in the trade or business of the furnishing or sale of gas through a local distribution system.

(h) [Reserved]

§ 1.46-4 Limitations with respect to certain persons.

(a) *Mutual savings institutions.* In the case of an organization to which section 593 applies (that is, a mutual saving bank, a cooperative bank, or a domestic building and loan association)—

(1) The qualified investment with respect to each section 38 property shall be 50 percent of the amount otherwise determined under § 1.46-3, and

(2) The \$25,000 amount specified in section 46(a)(2)(A) and (B), relating to limitation based on amount of tax, shall be reduced by 50 percent of such amount.

For example, if a domestic building and loan association places in service on January 1, 1963, new section 38 property with a basis of \$30,000 and an estimated useful life of 6 years, its qualified investment for 1963 with respect to such property computed under § 1.46-3 is \$20,000 (66⅔ percent of \$30,000). However, under this paragraph such amount is reduced to \$10,000 (50 percent of \$20,000). If an organization to which section 593 applies is a member of an affiliated group (as defined in section 46(a)(5)), the \$25,000 amount specified in section 46(a)(2)(A) and (B) shall be reduced in accordance with the provisions of paragraph (f) of § 1.46-1 before such amount is further reduced under this paragraph.

(b) *Regulated investment companies and real estate investment trusts.* (1) In the case of a regulated investment company or a real estate investment trust subject to taxation under subchapter M, chapter 1 of the Code—

(i) The qualified investment with respect to each section 38 property otherwise determined under § 1.46-3, and

(ii) The \$25,000 amount specified in section 46(a)(2)(A) and (B), relating to limitation based on amount of tax,

shall be reduced to such person's ratable share of each such amount. If a regulated investment company or a real estate investment trust is a member of an affiliated group (as defined in section 46(a)(5)), the \$25,000 amount specified in section 46(a)(2)(A) and (B) shall be reduced in accordance with the provisions of paragraph (f) of § 1.46-1 before such amount is further reduced under this paragraph.

(2) A person's ratable share of the amount described in subparagraph (1)(i) and the amount described in subparagraph (1)(ii) of this paragraph shall be the ratio which—

(i) Taxable income for the taxable year, bears to

(ii) Taxable income for the taxable year plus the amount of the deduction for dividends paid taken into account under section 852(b)(2)(D) in computing investment company taxable income, or under section 857(b)(2)(C) in computing real estate investment trust taxable income, as the case may be.

For purposes of the preceding sentence, taxable income means, in the case of a regulated investment company its investment company taxable income (within the meaning of section 852(b)(2)), and in the case of a real estate investment trust its real estate investment trust taxable income (within the meaning of section 857(b)(2)). For purposes of this paragraph only, in computing taxable income for a taxable year beginning before January 1, 1964, a regulated investment company or a real estate investment trust may compute depreciation deductions with respect to section 38 property placed in service before January 1, 1964, without regard to the reduction in basis of such property required under § 1.48-7.

(3) This paragraph may be illustrated by the following example:

Example. (1) Corporation X, a regulated investment company subject to taxation under section 852 of the Code which makes its return on the basis of the calendar year, places in service on January 1, 1964, section 38 property with a basis of \$30,000 and an estimated useful life of 6 years. Corporation X's investment company taxable income under section 852(b)(2) is \$10,000 after taking into account a deduction for dividends paid of \$90,000.

(2) Under this paragraph, corporation X's qualified investment for the taxable year 1964 with respect to such property is \$2,000, computed as follows: (a) \$20,000 (qualified investment under § 1.46-3), multiplied by (b) \$10,000 (taxable income), divided by (c) \$100,000 (taxable income plus the deduction for dividends paid). For 1964, the \$25,000 amount specified in section 46(a)(2)(A) and (B) is reduced to \$2,500.

(c) *Cooperatives.* (1) In the case of a cooperative organization described in section 1381(a)—

(i) The qualified investment with respect to each section 38 property otherwise determined under § 1.46-3, and

(ii) The \$25,000 amount specified in section 46(a)(2)(A) and (B), relating to limitation based on amount of tax,

shall be reduced to such cooperative's ratable share of each such amount. If a cooperative organization described in section 1381(a) is a member of an affiliated group (as defined in section 46(a)(5)), the \$25,000 amount specified in section 46(a)(2)(A) and (B) shall be reduced in accordance with the provisions of paragraph (f) of § 1.46-1 before such amount is further reduced under this paragraph.

(2) A cooperative's ratable share of the amount described in subparagraph (1)(i) and the amount described in subparagraph (1)(ii) of this paragraph shall be the ratio which—

(i) Taxable income for the taxable year, bears to

(ii) Taxable income for the taxable year plus the sum of (a) the amount of the deductions allowed under section 1382(b), (b) the amount of the deduc-

tions allowed under section 1382(c), and (c) amounts similar to the amounts described in (a) and (b) of this subdivision the tax treatment of which is determined without regard to subchapter T, chapter 1 of the Code and the regulations thereunder.

Amounts similar to deductions allowed under section 1382 (b) or (c) are, for example, in the case of a taxable year of a cooperative organization beginning before January 1, 1963, the amount of patronage dividends which are excluded or deducted and any nonpatronage distributions which are deducted under section 522(b)(1). In the case of a taxable year of a cooperative organization beginning after December 31, 1962, such amounts are the amount of patronage dividends and nonpatronage distributions which are excluded or deducted without regard to section 1382 (b) or (c) because they are paid with respect to patronage occurring before 1963. For purposes of this paragraph only, in computing taxable income for a taxable year beginning before January 1, 1964, a cooperative may compute depreciation deductions with respect to section 38 property placed in service before January 1, 1964, without regard to the reduction in basis of such property required under § 1.48-7.

(3) This paragraph may be illustrated by the following example:

Example. (1) Cooperative X, an organization described in section 1381(a) which makes its return on the basis of the calendar year, places in service on January 1, 1964, section 38 property with a basis of \$30,000 and an estimated useful life of 6 years. Cooperative X's taxable income is \$10,000 after taking into account deductions of \$20,000 allowed under section 1382(b), deductions of \$60,000 allowed under section 1382(c), and deductions of \$10,000 allowed under section 522(b)(1)(B).

(2) Under this paragraph, cooperative X's qualified investment for the taxable year 1964 with respect to such property is \$2,000, computed as follows: (a) \$20,000 (qualified investment under § 1.46-3), multiplied by (b) \$10,000 (taxable income), divided by (c) \$100,000 (taxable income plus the sum of the deductions allowed under sections 1382(b), 1382(c), and 522(b)(1)(B)). For 1964, the \$25,000 amount specified in section 46(a)(2)(A) and (B) is reduced to \$2,500.

§ 1.47 Statutory provisions; certain dispositions, etc., of section 38 property.

Sec. 47. Certain dispositions, etc., of section 38 property—(a) General rule. Under regulations prescribed by the Secretary or his delegate—

(1) *Early disposition, etc.* If during any taxable year any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, before the close of the useful life which was taken into account in computing the credit under section 38, then the tax under this chapter for such taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior taxable years which would have resulted solely from substituting, in determining qualified investment, for such useful life the period beginning with the time such property was placed in service by the taxpayer and ending with the time such property ceased to be section 38 property.

(2) *Property becomes public utility property.* If during any taxable year any property taken into account in determining

qualified investment becomes public utility property (within the meaning of section 46(c)(3)(B)), then the tax under this chapter for such taxable year shall be increased by an amount equal to the aggregate decrease in the credits allowed under section 38 for all prior taxable years which would have resulted solely from treating the property, for purposes of determining qualified investment, as public utility property (after giving due regard to the period before such change in use). If the application of this paragraph to any property is followed by the application of paragraph (1) to such property, proper adjustment shall be made in applying paragraph (1).

(3) *Carrybacks and carryovers adjusted.* In the case of any cessation described in paragraph (1) or any change in use described in paragraph (2), the carrybacks and carryovers under section 46(b) shall be adjusted by reason of such cessation (or change in use).

(4) *Property destroyed by casualty, etc.* No increase shall be made under paragraph (1) and no adjustment shall be made under paragraph (3) in any case in which—

(A) Any property is disposed of, or otherwise ceases to be section 38 property with respect to the taxpayer, on account of its destruction or damage by fire, storm, shipwreck, or other casualty, or by reason of its theft;

(B) Section 38 property is placed in service by the taxpayer to replace the property described in subparagraph (A), and

(C) The reduction in basis or cost of such section 38 property described in the first sentence of section 46(c)(4) is equal to or greater than the reduction in qualified investment which (but for this paragraph) would be made by reason of the substitution required by paragraph (1) with respect to the property described in subparagraph (A).

(b) *Section not to apply in certain cases.* Subsection (a) shall not apply to—

(1) A transfer by reason of death, or

(2) A transaction to which section 381(a) applies.

For purposes of subsection (a), property shall not be treated as ceasing to be section 38 property with respect to the taxpayer by reason of a mere change in the form of conducting the trade or business so long as the property is retained in such trade or business as section 38 property and the taxpayer retains a substantial interest in such trade or business.

(c) *Special rule.* Any increase in tax under subsection (a) shall not be treated as tax imposed by this chapter for purposes of determining the amount of any credit allowable under subpart A.

[Sec. 47 as added by sec 2(b), Rev. Act 1962 (76 Stat. 963)]

§ 1.47-1 [Reserved]

§ 1.48 Statutory provisions; definitions; special rules.

Sec. 48. *Definitions; special rules—(a) Section 38 property—(1) In general.* Except as provided in this subsection, the term "section 38 property" means—

(A) Tangible personal property, or

(B) Other tangible property (not including a building and its structural components) but only if such property—

(i) Is used as an integral part of manufacturing, production, or extraction or of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services, or

(ii) Constitutes a research or storage facility used in connection with any of the activities referred to in clause (i), or

(C) Elevators and escalators, but only if—

(i) The construction, reconstruction, or erection of the elevator or escalator is completed by the taxpayer after June 30, 1963, or

(ii) The elevator or escalator is acquired after June 30, 1963, and the original use of such elevator or escalator commences with the taxpayer and commences after such date. Such term includes only property with respect to which depreciation (or amortization in lieu of depreciation) is allowable and having a useful life (determined as of the time such property is placed in service) of 4 years or more.

(2) *Property used outside the United States—(A) In general.* Except as provided in subparagraph (B), the term "section 38 property" does not include property which is used predominantly outside the United States.

(B) *Exceptions.* Subparagraph (A) shall not apply to—

(i) Any aircraft which is registered by the Administrator of the Federal Aviation Agency and which is operated to and from the United States;

(ii) Rolling stock, of a domestic railroad corporation subject to part I of the Interstate Commerce Act, which is used within and without the United States;

(iii) Any vessel documented under the laws of the United States which is operated in the foreign or domestic commerce of the United States;

(iv) Any motor vehicle of a United States person (as defined in section 7701(a)(30)) which is operated to and from the United States;

(v) Any container of a United States person which is used in the transportation of property to and from the United States; and

(vi) Any property (other than a vessel or an aircraft) of a United States person which is used for the purpose of exploring for, developing, removing, or transporting resources from the outer Continental Shelf (within the meaning of section 2 of the Outer Continental Shelf Lands Act, as amended and supplemented; 43 U.S.C., sec. 1331).

(3) *Property used for lodging.* Property which is used predominantly to furnish lodging or in connection with the furnishing of lodging shall not be treated as section 38 property. The preceding sentence shall not apply to—

(A) Nonlodging commercial facilities which are available to persons not using the lodging facilities on the same basis as they are available to persons using the lodging facilities; and

(B) Property used by a hotel or motel in connection with the trade or business of furnishing lodging where the predominant portion of the accommodations is used by transients.

(4) *Property used by certain tax-exempt organizations.* Property used by an organization (other than a cooperative described in section 521) which is exempt from the tax imposed by this chapter shall be treated as section 38 property only if such property is used predominantly in an unrelated trade or business the income of which is subject to tax under section 511.

(5) *Property used by governmental units.* Property used by the United States, any State or political subdivision thereof, any international organization, or any agency or instrumentality of any of the foregoing shall not be treated as section 38 property.

(6) *Livestock.* Livestock shall not be treated as section 38 property.

(b) *New section 38 property.* For purposes of this subpart, the term "new section 38 property" means section 38 property—

(1) The construction, reconstruction, or erection of which is completed by the taxpayer after December 31, 1961, or

(2) Acquired after December 31, 1961, if the original use of such property commences with the taxpayer and commences after such date.

In applying section 46(c)(1)(A) in the case of property described in paragraph (1), there

shall be taken into account only that portion of the basis which is properly attributable to construction, reconstruction, or erection after December 31, 1961.

(c) *Used section 38 property—(1) In general.* For purposes of this subpart, the term "used section 38 property" means section 38 property acquired by purchase after December 31, 1961, which is not new section 38 property. Property shall not be treated as "used section 38 property" if, after its acquisition by the taxpayer, it is used by a person who used such property before such acquisition (or by a person who bears a relationship described in section 179(d)(2)(A) or (B) to a person who used such property before such acquisition).

(2) *Dollar limitation—(A) In general.* The cost of used section 38 property taken into account under section 46(c)(1)(B) for any taxable year shall not exceed \$50,000. If such cost exceeds \$50,000, the taxpayer shall select (at such time and in such manner as the Secretary or his delegate shall by regulations prescribe) the items to be taken into account, but only to the extent of an aggregate cost of \$50,000. Such a selection, once made, may be changed only in the manner, and to the extent, provided by such regulations.

(B) *Married individuals.* In the case of a husband or wife who files a separate return, the limitation under subparagraph (A) shall be \$25,000 in lieu of \$50,000. This subparagraph shall not apply if the spouse of the taxpayer has no used section 38 property which may be taken into account as qualified investment for the taxable year of such spouse which ends within or with the taxpayer's taxable year.

(C) *Affiliated groups.* In the case of an affiliated group, the \$50,000 amount specified under subparagraph (A) shall be reduced for each member of the group by apportioning \$50,000 among the members of such group in accordance with their respective amounts of used section 38 property which may be taken into account.

(D) *Partnerships.* In the case of a partnership, the limitation contained in subparagraph (A) shall apply with respect to the partnership and with respect to each partner.

(3) *Definitions.* For purposes of this subsection—

(A) *Purchase.* The term "purchase" has the meaning assigned to such term by section 179(d)(2).

(B) *Cost.* The cost of used section 38 property does not include so much of the basis of such property as is determined by reference to the adjusted basis of other property held at any time by the person acquiring such property. If property is disposed of (other than by reason of its destruction or damage by fire, storm, shipwreck, or other casualty, or its theft) and used section 38 property similar or related in service or use is acquired as a replacement therefor in a transaction to which the preceding sentence does not apply, the cost of the used section 38 property acquired shall be its basis reduced by the adjusted basis of the property replaced. The cost of used section 38 property shall not be reduced with respect to the adjusted basis of any property disposed of if, by reason of section 47, such disposition involved an increase of tax or a reduction of the unused credit carrybacks or carryovers described in section 46(b).

(C) *Affiliated group.* The term "affiliated group" has the meaning assigned to such term by section 1504(a), except that—

(i) The phrase "more than 50 percent" shall be substituted for the phrase "at least 80 percent" each place it appears in section 1504(a), and

(ii) All corporations shall be treated as includible corporations (without any exclusion under section 1504(b)).

(d) *Certain leased property.* A person (other than a person referred to in section

46(d)) who is a lessor of property may (at such time, in such manner, and subject to such conditions as are provided by regulations prescribed by the Secretary or his delegate) elect with respect to any new section 38 property to treat the lessee as having acquired such property for an amount equal to—

- (1) Except as provided in paragraph (2), the fair market value of such property, or
- (2) If such property is leased by a corporation which is a member of an affiliated group (within the meaning of section 46(a)(5)) to another corporation which is a member of the same affiliated group, the basis of such property to the lessor.

The election provided by the preceding sentence may be made only with respect to property which would be new section 38 property if acquired by the lessee. For purposes of the preceding sentence and section 46(c), the useful life of property in the hands of the lessee is the useful life of such property in the hands of the lessor. If a lessor makes the election provided by this subsection with respect to any property, the lessee shall be treated for all purposes of this subpart as having acquired such property.

(e) *Subchapter S corporations.* In the case of an electing small business corporation (as defined in section 1371)—

- (1) The qualified investment for each taxable year shall be apportioned pro rata among the persons who are shareholders of such corporation on the last day of such taxable year; and

- (2) Any person to whom any investment has been apportioned under paragraph (1) shall be treated (for purposes of this subpart) as the taxpayer with respect to such investment, and such investment shall not (by reason of such apportionment) lose its character as an investment in new section 38 property or used section 38 property, as the case may be.

(f) *Estates and trusts.* In the case of an estate or trust—

- (1) The qualified investment for any taxable year shall be apportioned between the estate or trust and the beneficiaries on the basis of the income of the estate or trust allocable to each.

- (2) Any beneficiary to whom any investment has been apportioned under paragraph (1) shall be treated (for purposes of this subpart) as the taxpayer with respect to such investment, and such investment shall not (by reason of such apportionment) lose its character as an investment in new section 38 property or used section 38 property, as the case may be, and

- (3) The \$25,000 amount specified under subparagraphs (A) and (B) of section 46(a)(2) applicable to such estate or trust shall be reduced to an amount which bears the same ratio to \$25,000 as the amount of the qualified investment allocated to the estate or trust under paragraph (1) bears to the entire amount of the qualified investment.

(g) [Deleted]

(h) *Gross reference.* For application of this subpart to certain acquiring corporations, see section 381(c)(23).

[Sec. 48 as added by sec. 2(b), Rev. Act 1962 (78 Stat. 968); as amended by sec. 203(a)(1) and (3)(A), (b), and (c), Rev. Act 1964 (78 Stat. 33, 34)]

§ 1.48-1 Definition of section 38 property.

(a) *In general.* Property which qualifies for the credit allowed by section 38 is known as "section 38 property". Except as otherwise provided in this section, the term "section 38 property" means property (1) with respect to which depreciation (or amortization in lieu of depreciation) is allowable to the

taxpayer, (2) which has an estimated useful life of 4 years or more (determined as of the time such property is placed in service), and (3) which is either (i) tangible personal property, (ii) other tangible property (not including a building and its structural components) but only if such other property is used as an integral part of manufacturing, production, or extraction, or as an integral part of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services by a person engaged in a trade or business of furnishing any such service, or is a research or storage facility used in connection with any of the foregoing activities, or (iii) an elevator or escalator which satisfies the conditions of section 48(a)(1)(C). The determination of whether property qualifies as section 38 property in the hands of the taxpayer for purposes of the credit allowed by section 38 must be made with respect to the first taxable year in which such property is placed in service by the taxpayer. See paragraph (d) of § 1.46-3. For the meaning of "estimated useful life", see paragraph (e) of § 1.46-3.

(b) *Depreciation allowable.* (1) Property is not section 38 property unless a deduction for depreciation (or amortization in lieu of depreciation) with respect to such property is allowable to the taxpayer for the taxable year. A deduction for depreciation is allowable if the property is of a character subject to the allowance for depreciation under section 167 and the basis (or cost) of the property is recovered through a method of depreciation, including, for example, the unit of production method and the retirement method as well as methods of depreciation which measure the life of the property in terms of years. If property is placed in service (within the meaning of paragraph (d) of § 1.46-3) in a trade or business (or in the production of income), but under the taxpayer's depreciation practice the period for depreciation with respect to such property begins in a taxable year subsequent to the taxable year in which such property is placed in service, then a deduction for depreciation shall be treated as allowable with respect to such property in the earlier taxable year (or years). Thus, for example, if a machine is placed in service in a trade or business in 1963, but the period for depreciation with respect to such machine begins in 1964, because the taxpayer uses an averaging convention (see § 1.167(a)-10) in computing depreciation, then, for purposes of determining whether the machine qualifies as section 38 property, a deduction for depreciation shall be treated as allowable in 1963.

(2) If, for the taxable year in which property is placed in service, a deduction for depreciation is allowable to the taxpayer only with respect to a part of such property, then only the proportionate part of the property with respect to which such deduction is allowable qualifies as section 38 property for the purpose of determining the amount of credit allowable under section 38. Thus, for example, if property is used 80 percent of the time in a trade or business and is used 20 percent of the time for

personal purposes, only 80 percent of the basis (or cost) of such property qualifies as section 38 property. Further, property does not qualify to the extent that a deduction for depreciation thereon is disallowed under section 274 (relating to disallowance of certain entertainment, etc., expenses).

(3) If the cost of property is not recovered through a method of depreciation but through a deduction of the full cost in one taxable year, for purposes of subparagraph (1) of this paragraph a deduction for depreciation with respect to such property is not allowable to the taxpayer. However, if an adjustment with respect to the income tax return for such taxable year requires the cost of such property to be recovered through a method of depreciation, a deduction for depreciation will be considered as allowable to the taxpayer.

(4) If depreciation sustained on property is not an allowable deduction for the taxable year but is added to the basis of property being constructed, reconstructed, or erected by the taxpayer, for purposes of subparagraph (1) of this paragraph a deduction for depreciation shall be treated as allowable for the taxable year with respect to the property on which depreciation is sustained. Thus, if \$1,000 of depreciation sustained with respect to property no. 1, which is placed in service in 1964 by taxpayer A, is not allowable to A as a deduction for 1964 but is added to the basis of property being constructed by A (property no. 2), for purposes of subparagraph (1) of this paragraph a deduction for depreciation shall be treated as allowable to A for 1964 with respect to property no. 1. However, the \$1,000 amount is not included in the basis of property no. 2 for purposes of determining A's qualified investment with respect to property no. 2. See paragraph (c)(1) of § 1.46-3.

(c) *Definition of tangible personal property.* If property is tangible personal property it may qualify as section 38 property irrespective of whether it is used as an integral part of an activity (or constitutes a research or storage facility used in connection with such activity) specified in paragraph (a) of this section. Local law shall not be controlling for purposes of determining whether property is or is not "tangible" or "personal". Thus, the fact that under local law property is held to be personal property or tangible property shall not be controlling. Conversely, property may be personal property for purposes of the investment credit even though under local law the property is considered to be a fixture and therefore real property. For purposes of this section, the term "tangible personal property" means any tangible property except land and improvements thereto, such as buildings or other inherently permanent structures (including items which are structural components of such buildings or structures). Thus, buildings, swimming pools, paved parking areas, wharves and docks, bridges, and fences are not tangible personal property. Tangible personal property includes all property (other than structural components) which is contained in or attached to a building. Thus, such prop-

erty as production machinery, printing presses, transportation and office equipment, refrigerators, grocery counters, testing equipment, display racks and shelves, and neon and other signs, which is contained in or attached to a building constitutes tangible personal property for purposes of the credit allowed by section 38. Further, all property which is in the nature of machinery (other than structural components of a building or other inherently permanent structure) shall be considered tangible personal property even though located outside a building. Thus, for example, a gasoline pump, hydraulic car lift, or automatic vending machine, although annexed to the ground, shall be considered tangible personal property.

(d) *Other tangible property*—(1) *In general.* In addition to tangible personal property, any other tangible property (but not including a building and its structural components) used as an integral part of manufacturing, production, or extraction, or as an integral part of furnishing transportation, communications, electrical energy, gas, water, or sewage disposal services by a person engaged in a trade or business of furnishing any such service, or which constitutes a research or storage facility used in connection with any of the foregoing activities, may qualify as section 38 property.

(2) *Manufacturing, production, and extraction.* For purposes of the credit allowed by section 38, the terms "manufacturing", "production", and "extraction" include the construction, reconstruction, or making of property out of scrap, salvage, or junk material, as well as from new or raw material, by processing, manipulating, refining, or changing the form of an article, or by combining or assembling two or more articles, and include the cultivation of the soil, the raising of livestock, and the mining of minerals. Thus, section 38 property would include, for example, property used as an integral part of the extracting, processing, or refining of metallic and nonmetallic minerals, including oil, gas, rock, marble, or slate; the construction of roads, bridges, or housing; the processing of meat, fish or other foodstuffs; the cultivation of orchards, gardens, or nurseries; the operation of sawmills, the production of lumber, lumber products or other building materials; the fabrication or treatment of textiles, paper, leather goods, or glass; and the rebuilding, as distinguished from the mere repairing, of machinery.

(3) *Transportation and communications businesses.* Examples of transportation businesses include railroads, airlines, bus companies, shipping or trucking companies, and oil pipeline companies. Examples of communications businesses include telephone or telegraph companies and radio or television broadcasting companies.

(4) *Integral part.* In order to qualify for the credit, property (other than tangible personal property and research or storage facilities used in connection with any of the activities specified in subparagraph (1) of this paragraph) must be used as an integral part of one

or more of the activities specified in subparagraph (1) of this paragraph. Property such as pavements, parking areas, inherently permanent advertising displays or inherently permanent outdoor lighting facilities, or swimming pools, although used in the operation of a business, ordinarily is not used as an integral part of any of such specified activities. Property is used as an integral part of one of the specified activities if it is used directly in the activity and is essential to the completeness of the activity. Thus, for example, in determining whether property is used as an integral part of manufacturing, all properties used by the taxpayer in acquiring or transporting raw materials or supplies to the point where the actual processing commences (such as docks, railroad tracks and bridges), or in processing raw materials into the taxpayer's final product, would be considered as property used as an integral part of manufacturing. Specific examples of property which normally would be used as an integral part of one of the specified activities are blast furnaces, oil and gas pipelines, railroad tracks and signals, telephone poles, broadcasting towers, oil derricks, and fences used to confine livestock. Property shall be considered used as an integral part of one of the specified activities if so used either by the owner of the property or by the lessee of the property.

(5) *Research or storage facilities.* If property (other than a building and its structural components) constitutes a research or storage facility and if it is used in connection with an activity specified in subparagraph (1) of this paragraph, such property may qualify as section 38 property even though it is not used as an integral part of such activity. Examples of research facilities include wind tunnels and test stands. Examples of storage facilities include oil and gas storage tanks and grain storage bins. Although a research or storage facility must be used in connection with, for example, a manufacturing process, the taxpayer-owner of such facility need not be engaged in the manufacturing process.

(e) *Definition of building and structural components.* (1) Buildings and structural components thereof do not qualify as section 38 property. The term "building" generally means any structure or edifice enclosing a space within its walls, and usually covered by a roof, the purpose of which is, for example, to provide shelter or housing, or to provide working, office, parking, display, or sales space. The term includes, for example, structures such as apartment houses, factory and office buildings, warehouses, barns, garages, railway or bus stations, and stores. Such term includes any such structure constructed by, or for, a lessee even if such structure must be removed, or ownership of such structure reverts to the lessor, at the termination of the lease. Such term does not include (i) a structure which is essentially an item of machinery or equipment, or (ii) an enclosure which is so closely combined with the machinery or equipment which it supports, houses, or serves that it must be replaced, retired, or abandoned contemporaneously with such

machinery or equipment, and which is depreciated over the life of such machinery or equipment. Thus, the term "building" does not include such structures as oil and gas storage tanks, grain storage bins, silos, fractionating towers, blast furnaces, coke ovens, brick kilns, and coal tipples.

(2) The term "structural components" includes such parts of a building as walls, partitions, floors, and ceilings, as well as any permanent coverings therefor such as panelling or tiling; windows and doors; all components (whether in, on, or adjacent to the building) of a central air conditioning or heating system, including motors, compressors, pipes and ducts; plumbing and plumbing fixtures, such as sinks and bathtubs; electric wiring and lighting fixtures; chimneys; stairs, escalators, and elevators, including all components thereof; sprinkler systems; fire escapes; and other components relating to the operation or maintenance of a building. However, the term "structural components" does not include machinery the sole justification for the installation of which is the fact that such machinery is required to meet temperature or humidity requirements which are essential for the operation of other machinery or the processing of materials or foodstuffs. Machinery may meet the "sole justification" test provided by the preceding sentence even though it incidentally provides for the comfort of employees, or serves, to an insubstantial degree, areas where such temperature or humidity requirements are not essential. For example, an air conditioning and humidification system installed in a textile plant in order to maintain the temperature or humidity within a narrow optimum range which is critical in processing particular types of yarn or cloth is not included within the term "structural components". For special rules with respect to an elevator or escalator, the construction, reconstruction, or erection of which is completed by the taxpayer after June 30, 1963, or which is acquired after June 30, 1963, and the original use of which commences with the taxpayer and commences after such date, see section 48(a)(1)(C) and the regulations thereunder.

(f) *Intangible property.* Intangible property, such as patents, copyrights, and subscription lists, does not qualify as section 38 property. The cost of intangible property, in the case of a patent or copyright, includes all costs of purchasing or producing the item patented or copyrighted. Thus, in the case of a motion picture or television film or tape, the cost of the intangible property includes manuscript and screenplay costs, the cost of wardrobe and set design, the salaries of cameramen, actors, directors, etc., and all other costs properly includible in the basis of such film or tape. In the case of a book, the cost of the intangible property includes all costs of producing the original copyrighted manuscript, including the cost of illustration, research, and clerical and stenographic help. However, if tangible depreciable property is used in the production of such intangible property, see paragraph (b)(4) of this section.

(g) *Property used outside the United States*—(1) *General rule.* (i) Except as provided in subparagraph (2) of this paragraph, the term "section 38 property" does not include property which is used predominantly outside the United States (as defined in section 7701(a)(9)) during the taxable year. The determination of whether property is used predominantly outside the United States during the taxable year shall be made by comparing the period of time in such year during which the property is physically located outside the United States with the period of time in such year during which the property is physically located within the United States. If the property is physically located outside the United States during more than 50 percent of the taxable year, such property shall be considered used predominantly outside the United States during that year. If property is placed in service after the first day of the taxable year, the determination of whether such property is physically located outside the United States during more than 50 percent of the taxable year shall be made with respect to the period beginning on the date on which the property is placed in service and ending on the last day of such taxable year.

(ii) Since the determination of whether a credit is allowable to the taxpayer with respect to any property may be made only with respect to the taxable year in which the property is placed in service by the taxpayer, property used predominantly outside the United States during the taxable year in which it is placed in service cannot qualify as section 38 property with respect to such taxpayer, regardless of the fact that the property is permanently returned to the United States in a later year. Furthermore, if property is used predominantly in the United States in the year in which it is placed in service by the taxpayer, and a credit under section 38 is allowed with respect to such property, but such property is thereafter in any one year used predominantly outside the United States, such property ceases to be section 38 property with respect to the taxpayer and is subject to the application of section 47.

(iii) This subparagraph applies whether property is used predominantly outside the United States by the owner of the property, or by the lessee of the property. If property is leased and if the lessor makes a valid election under § 1.48-4 to treat the lessee as having purchased such property for purposes of the credit allowed by section 38, the determination of whether such property is physically located outside the United States during more than 50 percent of the taxable year shall be made with respect to the taxable year of the lessee; however, if the lessor does not make such an election, such determination shall be made with respect to the taxable year of the lessor.

(2) *Exceptions.* The provisions of subparagraph (1) of this paragraph do not apply to—

(i) Any aircraft which is registered by the Administrator of the Federal Aviation Agency and which is operated, whether on a scheduled or nonscheduled

basis, to and from the United States. The term "to and from the United States" is not intended to exclude an aircraft which makes flights from one point in a foreign country to another such point, as long as such aircraft returns to the United States with some degree of frequency;

(ii) Rolling stock, of a domestic railroad corporation subject to part I of the Interstate Commerce Act, which is used within and without the United States. For purposes of this subparagraph, the term "rolling stock" means locomotives, freight and passenger train cars, floating equipment, and miscellaneous transportation equipment on wheels, the expenditures for which are chargeable (or, in the case of leased property, would be chargeable) to the equipment investment accounts in the uniform system of accounts for railroad companies prescribed by the Interstate Commerce Commission;

(iii) Any vessel documented under the laws of the United States which is operated in the foreign or domestic commerce of the United States. A vessel is documented under the laws of the United States if it is registered, enrolled, or licensed under the laws of the United States by the Commissioner of Customs. Vessels operated in the foreign or domestic commerce of the United States include those documented for use in foreign trade, coastwise trade, or fisheries;

(iv) Any motor vehicle of a United States person (as defined in section 7701(a)(30)) which is operated to and from the United States with some degree of frequency;

(v) Any container of a United States person which is used in the transportation of property to and from the United States;

(vi) Any property (other than a vessel or an aircraft) of a United States person which is used for the purpose of exploring for, developing, removing, or transporting resources from the outer Continental Shelf (within the meaning of section 2 of the Outer Continental Shelf Lands Act, as amended and supplemented; 43 U.S.C., sec. 1331). Thus, for example, offshore drilling equipment may be section 38 property.

(h) *Property used for lodging*—(1). *In general.* (i) Except as provided in subparagraph (2) of this paragraph, the term "section 38 property" does not include property which is used predominantly to furnish lodging or is used predominantly in connection with the furnishing of lodging during the taxable year. Property used in the living quarters of a lodging facility, including beds and other furniture, refrigerators, ranges, and other equipment, shall be considered as used predominantly to furnish lodging. The term "lodging facility" includes an apartment house, hotel, motel, dormitory, or any other facility (or part of a facility) where sleeping accommodations are provided and let, except that such term does not include a facility used primarily as a means of transportation (such as an aircraft, vessel, or a railroad car) or used primarily to provide medical or convalescent services, even though sleeping accommodations are provided.

(ii) Property which is used predominantly in the operation of a lodging facility or in serving tenants shall be considered used in connection with the furnishing of lodging, whether furnished by the owner of the lodging facility or another person. Thus, for example, lobby furniture, office equipment, and laundry and swimming pool facilities used in the operation of an apartment house or in serving tenants would be considered used predominantly in connection with the furnishing of lodging. However, property which is not owned by or leased to the management of a lodging facility and which is not used directly by either the management or the tenants shall not be treated as property used in connection with the furnishing of lodging. However, property which is used in furnishing, to the management of a lodging facility or its tenants, electrical energy, water, sewage disposal services, gas, telephone service, or other similar services shall not be treated as property used in connection with the furnishing of lodging. Thus, such items as gas and electric meters, telephone poles and lines, telephone station and switchboard equipment, and water and gas mains, furnished by a public utility would not be considered as property used in connection with the furnishing of lodging.

(2) *Exceptions*—(i) *Nonlodging commercial facility.* A nonlodging commercial facility which is available to persons not using the lodging facility on the same basis as it is available to the tenants of the lodging facility shall not be treated as property which is used predominantly to furnish lodging or predominantly in connection with the furnishing of lodging. Examples of nonlodging commercial facilities include restaurants, drug stores, grocery stores, and vending machines located in a lodging facility.

(ii) *Property used by a hotel or motel.* Property used by a hotel, motel, inn, or other similar establishment, in connection with the trade or business of furnishing lodging shall not be considered as property which is used predominantly to furnish lodging or predominantly in connection with the furnishing of lodging, provided that the predominant portion of the living accommodations in the hotel, motel, etc., is used by transients during the taxable year. For purposes of the preceding sentence, the term "predominant portion" means "more than one-half". Thus, if more than one-half of the living quarters of a hotel, motel, inn, or other similar establishment is used during the taxable year to accommodate tenants on a transient basis, none of the property used by such hotel, motel, etc., in the trade or business of furnishing lodging shall be considered as property which is used predominantly to furnish lodging or predominantly in connection with the furnishing of lodging. Accommodations shall be considered used on a transient basis if the rental period is normally less than 30 days.

(i) [Reserved]

(j) *Property used by certain tax-exempt organizations.* The term "section 38 property" does not include property used by an organization (other than

a cooperative described in section 521) which is exempt from the tax imposed by chapter 1 of the Code unless such property is used predominantly in an unrelated trade or business the income of which is subject to tax under section 511. The term "property used by an organization" means (1) property owned by the organization (whether or not leased to another person), and (2) property leased to the organization. Thus, for example, a data processing or copying machine which is leased to an organization exempt from tax would be considered as property used by such organization. Property (unless used predominantly in an unrelated trade or business) leased by another person to an organization exempt from tax or leased by such an organization to another person is not section 38 property to either the lessor or the lessee, and in either case the lessor may not elect under § 1.48-4 to treat the lessee of such property as having purchased such property for purposes of the credit allowed by section 38. This paragraph shall not apply to property leased on a casual or short-term basis to an organization exempt from tax.

(k) *Property used by governmental units.* The term "section 38 property" does not include property used by the United States, any State (including the District of Columbia) or political subdivision thereof, any international organization (as defined in section 7701 (a)(18)), or any agency or instrumentality of the United States, of any State or political subdivision thereof, or of any international organization. The term "property used by the United States, etc." means (1) property owned by any such governmental unit (whether or not leased to another person), and (2) property leased to any such governmental unit. Thus, for example, a data processing or copying machine which is leased to any such governmental unit would be considered as property used by such governmental unit. Property leased by another person to any such governmental unit or leased by such governmental unit to another person is not section 38 property to either the lessor or the lessee, and in either case the lessor may not elect under § 1.48-4 to treat the lessee of such property as having purchased such property for purposes of the credit allowed by section 38. This paragraph shall not apply to property leased on a casual or short-term basis to any such governmental unit.

(l) *Livestock.* The term "section 38 property" does not include livestock. The term "livestock" includes horses, cattle, hogs, sheep, goats, and mink and other fur-bearing animals, irrespective of the use to which they are put or the purpose for which they are held.

§ 1.48-2 New section 38 property.

(a) *In general.* Section 48(b) defines "new section 38 property" as section 38 property—

(1) The construction, reconstruction, or erection of which is completed by the taxpayer after December 31, 1961, or

(2) Which is acquired by the taxpayer after December 31, 1961, provided

that the original use of such property commences with the taxpayer and commences after such date.

In the case of construction, reconstruction, or erection of such property commenced before January 1, 1962, and completed after December 31, 1961, there shall be taken into account as the basis of new section 38 property in determining qualified investment only that portion of the basis which is properly attributable to construction, reconstruction, or erection after December 31, 1961. See § 1.48-1 for the definition of section 38 property.

(b) *Special rules for determining date of acquisition, original use, and basis attributable to construction, reconstruction, or erection.* For purposes of paragraph (a) of this section, the principles set forth in paragraph (a) (1) and (2) of § 1.167(c)-1 shall be applied. Thus, for example, the following rules are applicable:

(1) Property is considered as constructed, reconstructed, or erected by the taxpayer if the work is done for him in accordance with his specifications.

(2) The portion of the basis of property attributable to construction, reconstruction, or erection after December 31, 1961, consists of all costs of construction, reconstruction, or erection allocable to the period after December 31, 1961, including the cost or other basis of materials entering into such work (but not including, in the case of reconstruction of property, the adjusted basis of the reconstructed property as of the time such reconstruction is commenced).

(3) It is not necessary that materials entering into construction, reconstruction, or erection be acquired after December 31, 1961, or that they be new in use.

(4) If construction or erection by the taxpayer began after December 31, 1961, the entire cost or other basis of such construction or erection may be taken into account as the basis of new section 38 property.

(5) Construction, reconstruction, or erection by the taxpayer begins when physical work is started on such construction, reconstruction, or erection.

(6) Property shall be deemed to be acquired when reduced to physical possession, or control.

(7) The term "original use" means the first use to which the property is put, whether or not such use corresponds to the use of such property by the taxpayer. For example, a reconditioned or rebuilt machine acquired by the taxpayer will not be treated as being put to original use by the taxpayer. The question of whether property is reconditioned or rebuilt property is a question of fact. Property will not be treated as reconditioned or rebuilt merely because it contains some used parts.

If the cost of reconstruction may properly either be capitalized and recovered through depreciation or charged against the depreciation reserve, such cost may be taken into account as the basis of new section 38 property even though it is charged against the depreciation reserve.

(c) *Examples.* This section may be illustrated by the following examples:

Example (1). If a machine with a total cost of \$100,000 is completed after December 31, 1961, and the portion attributable to construction by the taxpayer after December 31, 1961, is determined by engineering estimates or by cost accounting records to be \$30,000, the \$30,000 amount shall be taken into account by the taxpayer in computing qualified investment in new section 38 property.

Example (2). In 1965, a taxpayer reconditions a machine, which he constructed and placed in service in 1962 and which has an adjusted basis in 1965 of \$10,000. The cost of reconditioning amounts to an additional \$20,000. The basis of the machine which shall be taken into account in computing qualified investment in new section 38 property for 1965 is \$20,000, whether he contracts to have it reconditioned or reconditions it himself, and irrespective of whether the materials used for reconditioning are new in use.

Example (3). In 1961, a taxpayer pays the entire purchase price of \$10,000 for section 38 property to be delivered in 1962. In 1962 he takes possession of the property and commences the original use of the asset in that year. The \$10,000 amount shall be taken into account in computing qualified investment in new section 38 property for 1962.

Example (4). A taxpayer, instead of reconditioning his old machine, buys a "factory reconditioned" or "rebuilt" machine in 1962 to replace it. The reconditioned or rebuilt machine is not new section 38 property since such taxpayer is not the first user of the machine. See, however, § 1.48-3 (relating to used section 38 property).

Example (5). In 1962, a taxpayer buys from X for \$20,000 an item of section 38 property which has been previously used by X. The taxpayer in 1962 makes an expenditure on the property of \$5,000 of the type that must be capitalized. Regardless of whether the \$5,000 is added to the basis of such property or is capitalized in a separate account, such amount shall be taken into account by the taxpayer in computing qualified investment in new section 38 property for 1962. No part of the \$20,000 purchase price may be taken into account for such purpose. See, however, § 1.48-3 (relating to used section 38 property).

§ 1.48-3 Used section 38 property.

(a) *In general.* (1) Section 48(c) provides that "used section 38 property" means section 38 property acquired by purchase after December 31, 1961, which is not "new section 38 property". See §§ 1.48-1 and 1.48-2, respectively, for definitions of section 38 property and new section 38 property. In determining whether property is acquired by purchase, the provisions of paragraph (c) (1) of § 1.179-3 shall apply, except that (i) "1961" shall be substituted for "1957", and (ii) the definition of "affiliated group" in paragraph (e) (6) of this section shall be substituted for the definition of such term in paragraph (e) of § 1.179-3.

(2) (i) Property shall not qualify as used section 38 property if, after its acquisition by the taxpayer, it is used by (a) a person who used such property before such acquisition, or (b) a person who bears a relationship described in section 179(d) (2) (A) or (B) to a person who used such property before such acquisition. Thus, for example, if property is used by a person and is later sold by him under a sale and lease-back ar-

agement, such property in the hands of the purchaser-lessor is not used section 38 property because the property, after its acquisition, is being used by the same person who used it before its acquisition. Similarly, where a lessee has been leasing property and subsequently purchases it (whether or not the lease contains an option to purchase), such property is not used section 38 property with respect to the purchaser because the property is being used by the same person who used it before its acquisition. In addition, if property owned by a lessor is sold subject to the lease, or is sold upon the termination of the lease, the property will not qualify as used section 38 property with respect to the purchaser if, after the purchase, the property is used by a person who used the property as a lessee before the purchase.

(ii) For purposes of applying subdivision (i) of this subparagraph, (a) property used by a partnership shall be considered as used by each partner, and (b) property shall not be considered as used by a person before its acquisition if such property was used only on a casual basis by such person.

(iii) In determining whether a person bears a relationship described in section 179(d)(2) (A) or (B) to a person who used property before its acquisition by the taxpayer, the provisions of paragraph (c)(1) (i) and (ii) of § 1.179-3 shall apply, except that the definition of "affiliated group" in paragraph (e)(6) of this section shall be substituted for the definition of such term in paragraph (e) of § 1.179-3.

(3) The provisions of this paragraph may be illustrated by the following examples:

Example (1). Corporation P acquires properties 1 and 2 in 1960 and uses them in its trade or business until 1962. In 1962, corporation P sells such properties to corporation Y, which leases back property 1 to corporation P and leases property 2 to corporation S, a wholly owned subsidiary of corporation P. Property 1 is not used section 38 property in the hands of corporation Y because, after its acquisition by corporation Y, it is used by a person (corporation P) who used it prior to such acquisition. Property 2 is not used section 38 property because, after its acquisition by corporation Y, it is used by a person (corporation S) who is related, within the meaning of section 179(d)(2)(B), to a person (corporation P) who used it before such acquisition.

Example (2). In 1962, corporation L leases property from corporation M. In 1964, corporation L acquires the property that it previously had been leasing. The property acquired by corporation L is not used section 38 property because such property is used after such acquisition by the same person (corporation L) who used the property before its acquisition (corporation L).

Example (3). Corporation X buys property in 1962 and leases such property to corporation Y. Corporation X in 1965 sells the property to A subject to the lease. The property acquired by A is not used section 38 property if such property continues to be used by corporation Y, because corporation Y used the property before its acquisition by A.

Example (4). A owns a bulldozer which he rents out to a number of different users, including B. In 1962, B used the bulldozer from February 16 to March 12 and again on October 15 and 16. B purchases the bulldozer from A on December 1, 1962. The prior use of the property by B does not disqualify such property as used section 38 property to B, because he used such property only on a casual basis prior to its purchase.

Example (5). C places machine 1 in service in his individually owned business during 1961. During 1963, C sells machine 1 to partnership CDE in which he shares one-third of the profits and losses. The machine is not used section 38 property to partnership CDE because it is used after acquisition by the same person (partner C) who used the property before acquisition. Similarly, if partnership CDE places machine 2 in service during 1961 and sells that machine to partner C during 1963, machine 2 would not be used section 38 property to partner C. Moreover, if F buys partner C's interest in partnership CDE, such acquisition would not result in the acquisition of used section 38 property by F (whether or not the optional adjustment to basis of partnership property provided by section 743 applies) because the partnership property is used, after F acquires his interest, by the same persons (partners D and E) who used the property before the acquisition.

(b) **Cost.** (1) The cost of used section 38 property is equal to the basis of such property, but does not include so much of such basis as is determined by reference to the adjusted basis of other property (whether or not section 38 property) held at any time by the taxpayer acquiring such used section 38 property. (2) If property (whether or not section 38 property) is disposed of by the taxpayer (other than by reason of its destruction or damage by fire, storm, shipwreck, or other casualty, or its theft) and used section 38 property similar or related in service or use is acquired as a replacement therefor in a transaction in which the basis of the replacement property is not determined by reference to the adjusted basis of the property replaced, then the cost of the used section 38 property so acquired shall be its basis reduced by the adjusted basis of the property replaced. The preceding sentence shall apply only if the taxpayer acquires (or enters into a contract to acquire) the replacement property within a period of 60 days before or after the date of the disposition.

(3) Notwithstanding subparagraphs (1) and (2) of this paragraph, the cost of used section 38 property shall not be reduced with respect to the adjusted basis of any property disposed of if, by reason of section 47, such disposition resulted in an increase of tax or a reduction of investment credit carrybacks or carryovers described in section 46(b). (4) The provisions of this paragraph may be illustrated by the following examples:

Example (1). In 1972, A acquires machine 2 (an item of used section 38 property which has a sales price of \$5,600) by trading in machine 1 (an item of section 38 property acquired in 1962), and by paying an additional \$4,000 cash. The adjusted basis of machine 1 is \$1,600. Under the provisions of sections 1012 and 1031(d), the basis of machine 2 is \$5,600 (\$1,600 adjusted basis of machine 1 plus cash expended of \$4,000). The cost of machine 2 which may be taken into account in computing qualified investment for 1972 is \$4,000 (basis of \$5,600 less \$1,600 adjusted basis of machine 1).

Example (2). The facts are the same as in example (1) except that machine 2 has a sales price of \$6,000. The trade-in allow-

ance on machine 1 is \$2,000. The result is the same as in example (1), that is, the basis of machine 2 is \$5,600 (\$1,600 plus \$4,000); therefore, the cost of machine 2 which may be taken into account in computing qualified investment for 1972 is \$4,000 (basis of \$5,600 less \$1,600 adjusted basis of machine 1).

Example (3). On September 18, 1962, B sells truck 1, which he acquired in 1961 and which has an adjusted basis in his hands of \$1,200. On October 15, 1962, he purchases for \$2,000 truck 2 (an item of used section 38 property) as a replacement therefor. The cost of truck 2 which may be taken into account in computing qualified investment is \$800 (\$2,000 less \$1,200).

Example (4). In 1962, C acquires property 1, an item of new section 38 property with a basis of \$12,000 and a useful life of eight years or more. He is allowed a credit under section 38 of \$840 (7 percent of \$12,000) with respect to such property. In 1968, C acquires property 2 (an item of used section 38 property) by trading in property 1 and by paying an additional amount in cash. Section 47(a) applies to the disposition of property 1 and C's tax liability for 1968 is increased by \$280. Since the application of section 47(a) results in an increase in tax, for purposes of computing qualified investment the cost of property 2 is not reduced by any part of the adjusted basis of the property traded in.

(c) **Dollar limitation.**—(1) *In general.* Section 48(c)(2) provides that the aggregate cost of used section 38 property which may be taken into account for any taxable year in computing qualified investment under section 46(c)(1)(B) shall not exceed \$50,000. If the total cost of used section 38 property exceeds \$50,000, there must be selected, in the manner provided in subparagraph (4) of this paragraph, the particular items of used section 38 property the cost of which is to be taken into account in computing qualified investment. The cost of used section 38 property that may be taken into account by a person in applying the \$50,000 limitation for any taxable year includes not only the cost of used section 38 property placed in service by such person during such taxable year, but also the cost of used section 38 property apportioned to such person. For purposes of this section, the cost of used section 38 property apportioned to any person means the cost of such property apportioned to him by a trust, estate, or electing small business corporation (as defined in section 1371(b)), and his share of the cost of partnership used section 38 property, with respect to the taxable year of such trust, estate, corporation or partnership ending with or within such person's taxable year. Thus, if an individual places in service during his taxable year used section 38 property with a cost of \$25,000, if the cost of used section 38 property apportioned to him by an electing small business corporation for such year is \$30,000, and if his share for such year of the cost of used section 38 property placed in service by a partnership is \$20,000, he may select from the used section 38 property with a total cost of \$75,000 the particular used section 38 property the cost of which he wishes to take into account. No part of the excess of \$25,000 (\$75,000 cost minus \$50,000 annual limitation) may be taken into account in any other taxable year. For determining the amount of the cost to be apportioned by an electing small business corpora-

tion, see paragraph (a)(2) of § 1.43-5; in the case of estates and trusts, see paragraph (a)(2) of § 1.43-6. See paragraph (e) of this section for application of \$50,000 limitation in the case of affiliated groups.

(2) *Married individuals filing separate returns.* In the case of a husband or wife who files a separate return, the aggregate cost of used section 38 property which may be taken into account for the taxable year to which such return relates cannot exceed \$25,000. The preceding sentence shall not apply, however, unless the taxpayer's spouse places in service (or is apportioned the cost of) used section 38 property for the taxable year of such spouse which ends with or within the taxpayer's taxable year. Thus, if a husband and wife who file separate returns on a calendar year basis both place in service used section 38 property during the taxable year, the maximum cost of used section 38 property which may be taken into account by each is \$25,000. However, in such case, if only one spouse places in service (or is apportioned the cost of) used section 38 property during the taxable year, such spouse may take into account a maximum of \$50,000 for such year. The determination of whether an individual is married shall be made under the principles of section 143 and the regulations thereunder.

(3) *Partnerships.* In the case of a partnership, the aggregate cost of used section 38 property placed in service by the partnership (or apportioned to the partnership) which may be taken into account by the partners with respect to any taxable year of the partnership may not exceed \$50,000. If such aggregate cost exceeds \$50,000, the partnership must make a selection in the manner provided in subparagraph (4) of this paragraph. The \$50,000 limitation applies to each partner, as well as to the partnership.

(4) *Selection of \$50,000 cost.* (i) If the sum of (a) the cost of used section 38 property placed in service during the taxable year by any person, (b) such person's share of the cost of partnership used section 38 property placed in service during the taxable year of a partnership ending with or within such person's taxable year, and (c) the cost of used section 38 property apportioned to such person for such taxable year by an electing small business corporation, estate, or trust, exceeds \$50,000, such person must make a selection for such taxable year in the manner provided in subdivision (ii) of this subparagraph.

(ii) For purposes of computing qualified investment (or, in the case of a partnership, electing small business corporation, estate, or trust, for purposes of selecting used section 38 property the cost of which may be taken into account by the partners, shareholders, or estate or trust and its beneficiaries) any person to whom subdivision (i) of this subparagraph applies must select a total cost of \$50,000 from (a) the cost of specific used

section 38 property placed in service by such person, (b) such person's share of the cost of specific used section 38 property placed in service by a partnership, and (c) the cost of used section 38 property apportioned to such person by an electing small business corporation, estate, or trust. When a particular property is selected, the entire cost (or entire share of cost of a particular property in the case of partnership property) of such property must be taken into account unless, as a result of the selection of such particular property, the \$50,000 limitation is exceeded. Likewise, in the case of an apportionment from an electing small business corporation, estate, or trust, when the cost in a particular useful life category is selected, the entire cost in such category must be taken into account unless, as a result of the selection of such cost, the \$50,000 limitation is exceeded. Thus, if a person places in service during the taxable year three items of used section 38 property, each with a cost of \$20,000, he must select the entire cost of two of the items and only \$10,000 of the cost of the third item; he may not select a portion of the cost of each of the three items. The selection by any person shall be made by taking the cost of used section 38 property into account in computing qualified investment (or in selecting the used section 38 property the cost of which may be taken into account by the partners, etc.), and if such property was placed in service by such person, he must maintain records which permit specific identification of any item of used section 38 property selected.

(5) *Examples.* The provisions of this paragraph may be illustrated by the following examples:

Example (1). H, who operates a sole proprietorship, purchases and places in service in 1963 used section 38 property with a cost of \$60,000. His spouse, W, is a shareholder in an electing small business corporation

which purchases and places in service during its fiscal year ending June 30, 1963, used section 38 property with a cost of \$50,000. Both spouses file separate returns on a calendar year basis. W, as a 60 percent shareholder on the last day of the taxable year of the corporation, is apportioned \$30,000 (60 percent of \$50,000) of the cost of the used section 38 property placed in service by the corporation. The cost of used section 38 property that may be taken into account by H on his separate return is \$25,000. The cost of used section 38 property that may be taken into account by W on her separate return is \$25,000. On the other hand, if the corporation had made no investment in used section 38 property, H could take \$50,000 of the \$60,000 cost into account.

Example (2). Partners X, Y, and Z share the profits and losses of partnership XYZ in the ratio of 50 percent, 30 percent, and 20 percent, respectively. The partnership and each partner make returns on the basis of the calendar year. Each partner also operates a sole proprietorship. In 1963, the partnership and the partners purchase and place in service the following used section 38 property:

Property	Estimated useful life	Cost
<i>Partnership XYZ</i>		
Property No. 1.....	9 years.....	\$10,000
Property No. 2.....	7 years.....	50,000
Property No. 3.....	7 years.....	50,000
Property No. 4.....	5 years.....	30,000
<i>Partner X</i>		
Property No. 5.....	6 years.....	30,000
<i>Partner Y</i>		
Property No. 6.....	10 years.....	60,000
<i>Partner Z</i>		
Property No. 7.....	4 years.....	36,000

(1) *Selection by partnership.* In accordance with subparagraph (4)(i) of this paragraph, the partnership selects property No. 1 and \$40,000 of the cost of property No. 2 to be taken into account. Therefore, each partner's share of cost of the property selected by the partnership is as follows:

Property No.	Estimated useful life	Selected cost	Partner's share of cost		
			X (50%)	Y (30%)	Z (20%)
1.....	9 years.....	\$10,000	\$5,000	\$3,000	\$2,000
2.....	7 years.....	40,000	20,000	12,000	8,000
Total.....		50,000	25,000	15,000	10,000

(ii) *Selection by partners.* In accordance with subparagraph (4)(ii) of this paragraph, the partners make the following selections: Partner X selects property No. 5 (\$30,000), his share of the cost of property No. 1 (\$5,000), and \$15,000 of his share of the cost of property No. 2. Partner Y selects \$50,000 of the cost of property No. 6, and no part of his share of the cost of partnership property. Partner Z, having an aggregate cost of used section 38 property of only \$46,000 (partnership property of \$10,000 and individually owned property of \$36,000), takes into account the entire \$46,000.

(iii) *Qualified investment of partner X.* X's total qualified investment in used section 38 property for 1963 is \$35,000, computed as follows:

Property No.	Estimated useful life	Selected cost	Applicable percentage	Qualified investment
1.....	9 years.....	\$5,000	100	\$5,000
2.....	7 years.....	15,000	66⅔	10,000
5.....	6 years.....	30,000	66⅔	20,000
Total.....		50,000		35,000

(iv) *Qualified investment of partner Y.* Y's total qualified investment in used section 38 property for 1963 is \$50,000 (100 percent of \$50,000) since he selected \$50,000 of the cost of property No. 6 which has a useful life of 8 years or more.

(v) *Qualified investment of partner Z.* Z's total qualified investment in used section 38 property for 1963 is \$19,333, computed as follows:

Property No.	Estimated useful life	Selected cost	Applicable percentage	Qualified investment
1	9 years	\$2,000	100	\$2,000
2	7 years	8,000	66 $\frac{2}{3}$	5,333
7	4 years	36,000	33 $\frac{1}{3}$	12,000
Total		46,000		19,333

(d) [Reserved]

(e) *Dollar limitation for members of an affiliated group.*—(1) *In general.* (i) Section 48(c)(2)(C) provides that the \$50,000 limitation on the cost of used section 38 property which may be taken into account for any taxable year shall, in the case of an affiliated group (as defined in subparagraph (6) of this paragraph), be reduced for each member of the group by apportioning the \$50,000 amount among those corporations which are the members of such group in accordance with their respective amounts of used section 38 property which may be taken into account, that is, in accordance with the total cost of used section 38 property placed in service by each member during its taxable year (without regard to the \$50,000 limitation or the applicable percentages to be applied in computing qualified investment).

(ii) Except as otherwise provided in this paragraph, the \$50,000 amount shall be apportioned among those corporations which are members of the affiliated group on the last day of the taxable year of the common parent. For the taxable year of each such member ending with, or within which falls, the last day of the taxable year of the common parent, the cost of used section 38 property taken into account in computing qualified investment under section 46(c)(1)(B) shall not exceed an amount which bears the same ratio to \$50,000 as (a) the cost of used section 38 property placed in service by such member for such taxable year, bears to (b) the total cost of used section 38 property placed in service by all members of the affiliated group for their taxable years ending with, or within which falls, such last day of the taxable year of the common parent.

(iii) There shall be attached to the common parent's income tax return a statement containing the name, address, and taxpayer account number of each member of the affiliated group as of the last day of the common parent's taxable year and a schedule showing the computation of the apportionment of the \$50,000 amount among members of the affiliated group. Each such member of the group shall retain as a part of its records a copy of the statement containing the apportionment schedule which is attached to the common parent's return. If the due date (including extensions of time) of the common parent's return is before July 15, 1964, the required statement may be filed on or before such date with the district director with whom the return was filed.

(iv) If a member of the affiliated group (including the common parent) makes its income tax return on the basis of a 52-53-week taxable year, the principles of section 441(f)(2)(A)(ii) and paragraph (b)(1) of § 1.441-2 apply in determining the last day of such a taxable year.

(2) *Estimate of used section 38 property to be placed in service.* (i) For purposes of subparagraph (1) of this paragraph, if the taxable year of a member of the affiliated group (within which falls the last day of the common parent's taxable year) ends later than the 30th day preceding the date on which the common parent's income tax return for such year is due (including extensions of time), such member shall use (if the total cost of used section 38 property actually placed in service during its taxable year is not known), as the cost of used section 38 property placed in service by it during its taxable year, an estimate of the cost of such property to be placed in service by it during such year. Such estimate shall be made on the basis of the facts and circumstances known as of the time of the estimate. Any such estimate shall also be used in determining the total cost of used section 38 property placed in service by all members of the affiliated group for their taxable years ending with, or within which falls, the last day of such taxable year of the common parent.

(ii) If an estimate is used by any member of an affiliated group pursuant to subdivision (i) of this subparagraph, each member may later file an original or amended return in which the apportionment of the \$50,000 amount is based upon the cost of used section 38 property actually placed in service by all members of the affiliated group during their taxable years which end with, or within which falls, the last day of the common parent's taxable year. Such amended apportionment shall be made only if the common parent, and each member of the group whose limitation would be changed, file original or amended returns which reflect the amended apportionment based upon the cost of the used section 38 property actually placed in service by the group. In such case, a new statement (reflecting the amended apportionment) shall be attached to the original or amended return of the common parent and a copy of such statement shall be retained by each such member pursuant to the requirements in subparagraph (1)(iii) of this paragraph.

(3) *Short taxable year.* If (i) the return of a corporation is for a short period, (ii) such corporation is a member of an affiliated group as of the last day of such period, and (iii) the last day of the taxable year of the common parent of the group does not end with or within such short period, then such corporation's taxable year shall, for purposes of this paragraph, be considered as ending with the last day of the common parent's taxable year within which falls such short period. Such corporation will thus be considered to be a member of the affiliated group as of the last day of the common parent's taxable year and may be apportioned part of the \$50,000

amount under subparagraph (1)(ii) of this paragraph. However, if such corporation's income tax return is due (including extensions of time) before the income tax return of the common parent is filed, then such corporation shall be considered to have placed no used section 38 property in service and no part of the \$50,000 amount shall be apportioned to such corporation unless such corporation files (on or after the date the common parent files its return) an amended return reflecting the cost of used section 38 property placed in service by it during its short period and such cost is taken into account by the common parent in apportioning the \$50,000 amount.

(4) *Two or more common parents.* If a corporation during its taxable year is a member of two or more affiliated groups as of the last day of the taxable year of the common parent of each such group, such corporation shall be considered to be a member of only the affiliated group whose common parent's taxable year ends earliest in such corporation's taxable year.

(5) *Nonresident foreign corporation.* (i) A foreign corporation not engaged in trade or business within the United States (hereinafter referred to in this subparagraph as a "nonresident foreign corporation") which is not a common parent need not retain as a part of its records a copy of the statement required by subparagraph (1)(iii) of this paragraph.

(ii) A nonresident foreign corporation which is a common parent of an affiliated group shall be considered to have a taxable year ending December 31.

(iii) If a nonresident foreign corporation is a common parent of an affiliated group, the statement required by subparagraph (1)(iii) (or (2)(ii)) of this paragraph shall be filed with the Director, International Operations Division, Internal Revenue Service, Washington, D.C., 20225. The statement required by subparagraph (1)(iii) shall be due on or before the 75th day after the end of its taxable year (as determined under subdivision (ii) of this subparagraph), or on or before July 15, 1964, whichever is later. For purposes of subparagraph (2) of this paragraph, this statement shall be considered the return of such corporation.

(6) *Definition of affiliated group.* For purposes of this section, an affiliated group means one defined in section 1504(a), except that (i) the phrase "more than 50 percent" shall be substituted for the phrase "at least 80 percent" each place it appears in section 1504(a), and (ii) all corporations shall be treated as includible corporations (without any exclusion under section 1504(b)). Thus, a foreign corporation or a corporation exempt from taxation under section 501 may be a member of an affiliated group for purposes of this section even though under section 1504(b) neither corporation would be an includible corporation.

(7) *Affiliated group filing a consolidated return.* For the purpose of apportioning the \$50,000 amount in the case of members of an affiliated group

which join in filing a consolidated return, all such members shall be treated as though they were a single member. Thus, in determining the limitation on the cost of used section 38 property which may be taken into account by the group filing the consolidated return, the apportionment provided in subparagraph (1) (i) of this paragraph shall be made by using the aggregate cost of such property placed in service by all members of the group filing the consolidated return. If all members of the affiliated group join in filing a consolidated return, the group may select the items to be taken into account to the extent of an aggregate cost of \$50,000; if some members of the affiliated group do not join in filing the consolidated return, then the members of the group which join in filing the consolidated return may select the items to be taken into account to the extent of the amount apportioned to such members under subparagraph (1) (i) of this paragraph.

(8) *Examples.* This paragraph may be illustrated by the following examples:

Example (1). (1) P, a domestic corporation, files an income tax return for its taxable year ending June 30, 1963, during which year it places in service used section 38 property with a cost of \$100,000. On June 30, 1963, P owns 51 percent of the outstanding stock of S, also a domestic corporation. S files a separate income tax return on the basis of a fiscal year ending July 31, 1963, during which year it places in service used section 38 property with a cost of \$150,000. The membership of the affiliated group is ascertained as of the close of June 30, 1963, the last day of the taxable year of the common parent, P. On that day the affiliated group consists of P and S.

(ii) The cost of used section 38 property taken into account by P for its taxable year ending June 30, 1963, may not exceed \$20,000, that is, an amount which bears the same ratio to \$50,000 as the cost of used section 38 property placed in service by P for its taxable year (\$100,000) bears to the total cost of used section 38 property placed in service by all members of the affiliated group (P and S) for their taxable years containing June 30, 1963 (\$250,000). Similarly, the cost of used section 38 property taken into account by S for its taxable year ending July 31, 1963, may not exceed \$30,000.

Example (2). (1) P, a domestic corporation, files an income tax return for its taxable year ending December 31, 1962, during which year it places in service used section 38 property costing \$100,000. On December 31, 1962, P owns all the outstanding stock of S, a domestic corporation which files a separate income tax return for the fiscal year ending September 30, 1963. P receives no extension of time for filing its return due March 15, 1963. Since the taxable year of S within which falls December 31, 1962 (the last day of P's taxable year) ends later than February 14, 1963 (the 30th day preceding the date on which P's return is due), S estimates the cost of used section 38 property which will be placed in service during its year. On the basis of the facts and circumstances known as of the time of the estimate, S estimates that it will place in service during such year used section 38 property costing \$150,000.

(ii) The cost of used section 38 property taken into account by P and S for their respective taxable years may not exceed \$20,000 $\left(\frac{\$100,000}{\$250,000} \times \$50,000\right)$ and \$30,000 $\left(\frac{\$150,000}{\$250,000} \times \$50,000\right)$, respectively. If S actually places in service during its taxable year used sec-

tion 38 property costing more or less than \$150,000, its income tax return for the year ending September 30, 1963, may reflect an amended apportionment of the \$50,000 limitation based upon the cost of used section 38 property actually placed in service by the group, provided that P files an amended return to reflect the amended apportionment. For example, if S places in service used section 38 property costing \$200,000, the cost of used section 38 property taken into account by P and S for their respective taxable years could not exceed \$16,667 $\left(\frac{\$100,000}{\$300,000} \times \$50,000\right)$ and \$33,333 $\left(\frac{\$200,000}{\$300,000} \times \$50,000\right)$, respectively, under an amended apportionment.

§ 1.48-4 Election of lessor of new section 38 property to treat lessee as purchaser.

(a) *In general.* Under section 48(d), a lessor of property may elect to treat the lessee of such property as having purchased such property for purposes of the credit allowed by section 38 if the following conditions are satisfied:

(1) The property must be "section 38 property" in the hands of the lessor; that is, it must be property with respect to which depreciation (or amortization in lieu of depreciation) is allowable to the lessor, it must have a useful life of 4 years or more in his hands, and in every other respect it must meet the requirements of § 1.48-1. Thus, for example, property leased by a municipality to a taxpayer for use in what is commonly known as an "industrial park" is not eligible for the election since, under paragraph (k) of § 1.48-1, property used by a governmental unit is not section 38 property. In addition, property used by the lessee predominantly outside the United States is not eligible for the election since, under paragraph (g) of § 1.48-1, such property is not section 38 property. For purposes of this subparagraph, if the lessor is an estate or trust, depreciation (or amortization in lieu of depreciation) will be considered allowable to the estate or trust even if it is apportioned to the beneficiaries or other persons.

(2) The property must be "new section 38 property" (within the meaning of § 1.48-2) in the hands of the lessor; that is, either (i) construction, reconstruction, or erection of the property must be completed by the lessor after December 31, 1961, or (ii) the property must be acquired by the lessor after December 31, 1961, and the original use of such property must commence with the lessor and after such date. See paragraph (b) of this section for the application of the rules relating to "original use" in the case of leased property.

(3) The property would constitute "new section 38 property" to the lessee if such lessee had actually purchased the property. Thus, the election is not available if the lessee is not the original user of the property. See paragraph (b) of this section for the application of the rules relating to "original use" in the case of leased property. See paragraph (d) of this section for the determination of the estimated useful life of leased property in the hands of the lessee.

(4) A statement of election to treat the lessee as a purchaser has been filed

in the manner and within the time provided in paragraph (f) or (g) of this section.

(5) The lessor is not a person referred to in section 46(d), that is, a mutual savings bank, cooperative bank, or domestic building and loan association to which section 593 applies; a regulated investment company or real estate investment trust subject to taxation under subchapter M, chapter 1 of the Code; or a cooperative organization described in section 1381(a).

(6) In the case of property possession of which is transferred by a lessor to a lessee before February 26, 1964, the lessor and lessee do not join in filing a consolidated income tax return for a period which includes the date on which possession of such property is transferred to the lessee.

The election may be made on a property-by-property basis or a general election may be made with respect to each taxable year of a particular lessee. If the conditions of this paragraph have been met, the lessee shall be treated as though he were the actual owner of the property for purposes of the credit allowed by section 38. Thus, the lessee shall be entitled to the credit allowed by section 38 with respect to such property for the taxable year in which he places such property in service, and the lessor shall not be entitled to a credit allowed by section 38 with respect to such property. Moreover, if the leased property is disposed of by the lessee, or if it otherwise ceases to be section 38 property in his hands, the property will be subject to the provisions of section 47 (relating to early dispositions, etc.).

(b) *Original use.* For purposes of this section only, the lessor and the lessee may both be considered as the original users of an item of leased property. The determination of whether the lessor qualifies as the original user of leased property shall be made under paragraph (b) (7) of § 1.48-2. The determination of whether the lessee qualifies as the original user of leased property shall be made, under paragraph (b) (7) of § 1.48-2, as if the lessee actually purchased the property. Thus, the lessee would not be considered the original user of the property if it has been previously used by the lessor or another person, or if it is reconstructed, rebuilt, or reconditioned property. However, the lessee would be considered the original user if he is the first person to use the property for its intended function. Thus, the fact that the lessor may have, for example, tested, stored, or attempted to lease the property to other persons will not preclude the lessee from being considered the original user.

(c) *Basis of leased property.*—(1) *General rule.* If a valid election is made under this section, the amount of qualified investment under section 46(c) with respect to the leased property shall be determined by reference to the basis of such property in the hands of the lessee as determined under subparagraph (2), or (3) of this paragraph, whichever is applicable.

(2) *Property transferred before February 26, 1964.* (i) In the case of leased

property possession of which is transferred to the lessee before February 26, 1964, unless subdivision (ii) of this subparagraph applies, the basis of the property in the hands of the lessee shall be the basis of the property in the hands of the lessor.

(ii) If the property was constructed by the lessor (or by a corporation which controls or is controlled by the lessor within the meaning of section 368(c)), the basis of the property in the hands of the lessee shall be an amount equal to the fair market value of such property on the date possession is transferred to the lessee. The term "constructed" shall be given its commonly accepted meaning, that is, to build, manufacture, or erect something which did not theretofore exist. Thus, reconstruction, rebuilding, or reconditioning does not constitute "construction". However, it is not necessary that the materials used in construction be new in use.

(3) *Property transferred after February 25, 1964.* (i) In the case of leased property possession of which is transferred to the lessee after February 25, 1964, unless subdivision (ii) of this subparagraph applies, the basis of the property in the hands of the lessee shall be an amount equal to the fair market value of such property on the date possession is transferred to the lessee.

(ii) If the property is leased by a corporation which is a member of an affiliated group (within the meaning of paragraph (f) (5) of § 1.46-1) to another corporation which is a member of the same affiliated group on the date possession of the property is transferred to the lessee, the basis of the property in the hands of the lessee shall be the basis of the property in the hands of the lessor.

(d) *Estimated useful life of leased property.* The estimated useful life to the lessee of property subject to the election shall be deemed to be the estimated useful life in the hands of the lessor for purposes of computing depreciation, regardless of the term of the lease. The lessor shall determine the estimated useful life of each leased property on an individual basis even though multiple asset accounts (including guideline class accounts described in Revenue Procedure 62-21) are used. However, in the case of assets similar in kind contained in a multiple asset account, the lessor shall assign to each of such assets the average useful life of such assets used in computing depreciation. Thus, for example, if during a taxable year a lessor leases 10 similar trucks with an average estimated useful life for depreciation purposes of 7 years, based on an estimated range of 6 to 8 years, he must assign a useful life of 7 years to each of the 10 trucks.

(e) *Lessor itself a lessee.* If the lessor of property is itself a lessee who is treated, under this section, as having purchased such property, and such lessor makes a valid selection under this section to treat the sublessee as a purchaser, then the basis and estimated useful life of such property in the hands of the sublessee shall be determined under paragraphs (c) and (d) of this section as if the original lessor had leased

the property directly to the sublessee on the date possession of the property is transferred to the sublessee. Thus, for example, if on March 1, 1964, corporation X leases property to corporation Y, which in turn subleases the property to individual A (who is the first person to use the property for its intended function), and if both X and Y make valid elections under this section, the basis of the property to A is equal to its fair market value on the date on which possession is transferred from Y to A (regardless of whether X and Y are members of the same affiliated group), and its estimated useful life to A is the estimated useful life in the hands of X.

(f) *Property-by-property election—*

(1) *Manner of making election.* The election of a lessor with respect to a particular property (or properties) shall be made by filing a statement with the lessee, signed by the lessor and including the written consent of the lessee, containing the following information:

(i) The name, address, and taxpayer account number of the lessor and the lessee;

(ii) The district director's office with which the income tax returns of the lessor and the lessee are filed;

(iii) A description of each property with respect to which the election is being made;

(iv) The date on which possession of the property (or properties) is transferred to the lessee;

(v) The estimated useful life category of the property (or properties) in the hands of the lessor, that is, 4 years or more but less than 6 years, 6 years or more but less than 8 years, or 8 years or more; except that, in the case of property possession of which is transferred to the lessee before January 1, 1964, the lessor may, at his option, use the estimated useful life of the property (or properties) in the hands of the lessor expressed in terms of years;

(vi) The basis of the leased property in the hands of the lessee (or sublessee) as determined under paragraph (c) of this section; and

(vii) If the lessor is itself a lessee, the name, address, and taxpayer account number of the original lessor, and the district director's office with which the income tax return of such original lessor is filed.

(2) *Time for making election.* The statement referred to in subparagraph (1) of this paragraph shall be filed with the lessee on or before the 60th day after possession of the property is transferred to the lessee, or on or before July 15, 1964, whichever is later.

(3) *Election is irrevocable.* An election under this paragraph shall be irrevocable as of the time the statement referred to in subparagraph (1) of this paragraph is filed with the lessee.

(g) *General election—*(1) *In general.* In lieu of making elections on a property-by-property basis in the manner and time prescribed in paragraph (f) of this section, a lessor may, with respect to a particular taxable year of a particular lessee, make a general election to treat such lessee as having purchased all properties possession of which is trans-

ferred under lease by the lessor to the lessee during such taxable year of the lessee. An election under this paragraph may be made only with respect to taxable years of a lessee ending after March 31, 1963, and only with respect to properties possession of which is transferred under lease to such lessee after such date.

(2) *Manner and time for making general election.* The general election of a lessor with respect to a taxable year of a lessee shall be made by filing a statement with the lessee, signed by the lessor and including the written consent of the lessee, on or before the 60th day after the first transfer under lease (during such year) to the lessee of possession of property eligible for the general election under subparagraph (1) of this paragraph, or on or before July 15, 1964, whichever is later. Such statement of general election shall contain:

(i) The name, address, and taxpayer account number of the lessor and the lessee;

(ii) The taxable year of the lessee with respect to which such general election is made;

(iii) The district director's office with which the income tax returns of the lessor and the lessee are filed;

(iv) If the lessor is itself a lessee, the name, address, and taxpayer account number of the original lessor, and the district director's office with which the income tax return of such original lessor is filed.

(3) *Election is irrevocable.* A general election under this paragraph shall be irrevocable as of the time the statement referred to in subparagraph (2) of this paragraph is filed with the lessee and shall be binding on the lessor and the lessee for the entire taxable year of the lessee with respect to which such general election is made.

(4) *Information requirement.* If a lessor, with respect to a taxable year of a lessee, makes a general election under this paragraph, such lessor shall provide such lessee, on or before the 60th day after the last day of the lessee's taxable year, or on or before July 15, 1964, whichever is later, with a statement (or statements) containing the information required by paragraph (f) (1) (iii), (iv), (v) and (vi) of this section with respect to all properties possession of which is transferred under lease by the lessor to the lessee during such taxable year.

(h) *Signature.* The statement referred to in paragraph (f) (1) or (g) (2) of this section shall not be valid unless signed by both the lessor and the lessee. The signature of the lessee shall constitute the consent of the lessee to the election. The statement shall be signed by the taxpayer or a duly authorized agent of the taxpayer. For purposes of this section, a facsimile signature may be used in lieu of a signature manually executed and, if used, shall be as binding as a signature manually executed.

(i) [Reserved]

(j) *Record requirements.* The lessor and the lessee shall keep as a part of their records the statement referred to in paragraph (f) (1), or the statements referred to in paragraphs (g) (2) and (g) (4), of this section. The lessor shall

attach to his income tax return a summary statement of all property leased during his taxable year with respect to which an election is made. However, if the due date of the return (including extensions of time) is before July 15, 1964, the summary statement may be filed on or before such date with the district director with whom the return has been filed. Such summary statement shall contain the following information: (1) The name, address, and taxpayer account number of the lessor; and (2) in numerical account number order, each lessee's account number, name, and address, the estimated useful life category of the property (or, if applicable, the estimated useful life expressed in years), and the basis or fair market value of the property, whichever is applicable.

(k) *Adjustment of rental deductions.*—(1) *In general.* The rules of this paragraph apply only to section 38 property placed in service before January 1, 1964, and with respect to any such property only for taxable years of a lessee beginning before January 1, 1964. If a lessor makes a valid election under this section with respect to property placed in service by the lessee before January 1, 1964, section 48(g) and § 1.48-7 (relating to adjustments to basis of property) shall not apply to the lessor with respect to such property. Thus, the lessor is not required to reduce under section 48(g) (1) the basis of such property. However, if such an election is made, the deductions otherwise allowable under section 162 to the lessee for amounts paid or accrued to the lessor under the lease shall be adjusted in the manner provided in this paragraph. For special adjustment for taxable years beginning after December 31, 1963, see section 203(a) (2) (B) of the Revenue Act of 1964 (78 Stat. 33).

(2) *Decrease in rental deduction.* (i) The deductions otherwise allowable under section 162 to the lessee for amounts paid or accrued to the lessor under the lease with respect to leased property placed in service before January 1, 1964, shall be decreased under subdivision (ii) or (iii) of this subparagraph, whichever is applicable, by an amount determined by reference to the credit earned on the leased property. The "credit earned" on the leased property is determined by multiplying the qualified investment (as defined in section 46(c)) with respect to such property by 7 percent. Thus, the credit earned (and the decrease in deductions) is determined without regard to the limitation based on tax which, under section 46(a) (2), may limit the amount of the credit the lessee may take into account in any one year.

(ii) If, in the case of property placed in service before January 1, 1964, the lessor, under paragraph (f) (1) (v) of this section, supplies the lessee with the useful life of such property expressed in years, then for each taxable year beginning before January 1, 1964, any part of which falls within a period beginning with the month in which the leased property is placed in service by the lessee and ending with the close of the estimated useful life of such property (as determined under paragraph (d) of this section), the lessee shall decrease the deduction otherwise allowable under section 162 for each such taxable year with respect to such property. The decrease for each such taxable year shall be equal to (a) the credit earned, divided by (b) the estimated useful life of the property (expressed in months), multiplied by (c) the number of calendar months in which the leased property was held by the lessee during such taxable year. Thus, if leased property with a basis of \$27,000 in the hands of a calendar-year lessee, and with an estimated useful life of 10 years, is placed in service by the lessee on July 15, 1963, the lessee must decrease his section 162 deduction with respect to the leased property for the taxable year 1963 by \$94.50 (\$1,890 credit earned, divided by 120, multiplied by 6).

(iii) If, in the case of property placed in service before January 1, 1964, the lessor, under paragraph (f) (1) (v) of this section, supplies the lessee with the useful life category of such property, then for each taxable year beginning before January 1, 1964, during a period equal to the shortest life of the useful life category used by the lessee in computing qualified investment under section 46(c) with respect to the leased property, the lessee shall decrease the deduction otherwise allowable under section 162 for such taxable year with respect to such property. The decrease for each such taxable year shall be equal to the credit earned divided by such shortest life, that is, 4, 6, or 8. Such decreases shall begin with the taxable year during which the lessee places the property in service. Thus, if leased property with a basis of \$30,000 to the lessee, and an estimated useful life falling within the 4 years or more but less than 6 years useful life category, is placed in service by the lessee within the lessee's taxable year ending December 31, 1962, the lessee must decrease his section 162 deduction with respect to the leased property for each of the taxable years 1962 and 1963 by \$175 (\$700 credit earned divided by 4).

(iv) To the extent that a required decrease, under subdivision (ii) or (iii) of this subparagraph, is not taken into account for any taxable year beginning before January 1, 1964, because the deduction otherwise allowable under section 162 for such taxable year with respect to the leased property is less than the required decrease for such taxable year, then the balance of the required decrease not taken into account for such taxable year shall decrease the amount otherwise allowable as a deduction under section 162 with respect to such property for the next succeeding taxable year (or years) beginning before January 1, 1964, if any, for which a deduction is allowable with respect to such property. Thus, if the required decrease with respect to leased property is \$200 for 1962 but the lessee's deduction otherwise allowable under section 162 for such taxable year with respect to such property is only \$50, the balance of \$150 must be applied in 1963 to decrease the deduction otherwise allowable to the lessee with respect to the leased property for such taxable year.

(v) See paragraph (b) of § 1.48-7 for reduction of basis in the case of an actual purchase of leased property by a lessee (in a taxable year of such lessee beginning before January 1, 1964) who has been treated as a purchaser of such property under this section.

(3) *Increase in rental deduction.* If, in any taxable year of a lessee beginning before January 1, 1964, section 47 applies (because of an early disposition, etc., of the leased property) to property which is subject to a valid election under this section, and if as a result of the application of section 47 the lessee's tax for the taxable year is increased or a credit carryback or carryover is adjusted, then an appropriate increase in the lessee's deduction otherwise allowable under section 162 for such taxable year with respect to the leased property shall be made.

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

Example (1). X Corporation is engaged in the business of manufacturing and leasing new and reconstructed equipment which in its hands has an estimated useful life of 12 years. After December 31, 1961, X Corporation constructs machine no. 1 at a cost of \$20,000 and reconstructs machine no. 2 at a cost of \$5,000. On February 15, 1962, Y Corporation, a calendar-year taxpayer, leases both machines from X Corporation and places them in service. The fair market value of machine no. 1 on the date on which possession is transferred to Y is \$25,200. Machine no. 1 would qualify as new section 38 property in Y's hands if it had been purchased by Y. If X elects to treat Y as the purchaser of machine no. 1, under paragraph (c) (2) (ii) of this section such machine will have a basis of \$25,200 in Y's hands. Under paragraph (f) (1) (v) of this section, X supplies Y with an estimated useful life of 12 years (expressed in years rather than useful life category) with respect to machine no. 1 for purposes of determining Y's qualified investment. Y's credit earned with respect to the property is \$1,764 (7 percent of \$25,200). Under paragraph (k) (2) (ii) of this section, Y's deduction attributable to the leased property for 1962 will be decreased by \$134.75 (credit earned of \$1,764, divided by 144, multiplied by 11), and for 1963 such deduction will be decreased by \$147 (\$1,764, divided by 144, multiplied by 12). The election is not available with respect to machine no. 2 since a reconstructed machine would not constitute new section 38 property if Y had purchased it. In such case, while X cannot make the election to treat Y as a purchaser, X would be entitled to a credit under section 38 based on its expenditure of \$5,000 as an investment in new section 38 property, since such amount represents cost of reconstruction after December 31, 1961.

Example (2). Assume the same facts as in example (1) except that under paragraph (f) (1) (v) of this section, X supplies Y with an estimated useful life category of 8 years or more (rather than an estimated useful life expressed in years) with respect to machine no. 1 for purposes of determining Y's qualified investment. Under paragraph (k) (2) (iii) of this section, Y's deduction attributable to the leased property will be decreased by \$220.50 (credit earned of \$1,764, divided by 8) for each of its taxable years 1962 and 1963.

§ 1.48-5 Electing small business corporations.

(a) *In general.* (1) In the case of an electing small business corporation (as defined in section 1371(b)), the basis of

"new section 38 property" and the cost of "used section 38 property" placed in service during the taxable year shall be apportioned pro rata among the persons who are shareholders of such corporation on the last day of such corporation's taxable year. Section 38 property shall not (by reason of such apportionment) lose its character as new section 38 property or used section 38 property, as the case may be. The estimated useful life of such property in the hands of a shareholder shall be deemed to be the estimated useful life of such property in the hands of the electing small business corporation. The bases of all new section 38 properties which have a useful life falling within a particular useful life category shall be aggregated; likewise, the cost of all used section 38 properties which have a useful life falling within a particular useful life category shall be aggregated. The total bases of new section 38 properties within each useful life category and the total cost of used section 38 properties within each useful life category shall be apportioned separately. The useful life categories are: (i) 4 years or more but less than 6 years; (ii) 6 years or more but less than 8 years; and (iii) 8 years or more. There shall be apportioned to each person who is a shareholder of the electing small business corporation on the last day of the taxable year of such corporation, for his taxable year in which or with which the taxable year of such corporation ends, his pro rata share of the total bases of new section 38 properties within each useful life category, and his pro rata share of the total cost of used section 38 properties within each useful life category. In determining who are shareholders of an electing small business corporation on the last day of its taxable year, the rules of paragraph (d)(1) of § 1.1371-1 and of paragraph (a)(2) of § 1.1373-1 shall apply.

(2) The total cost of used section 38 property that may be apportioned by an electing small business corporation to its shareholders for any taxable year of such corporation shall not exceed \$50,000. If the total cost of used section 38 property placed in service during the taxable year by the electing small business corporation exceeds \$50,000 such corporation must select, under paragraph (c)(4) of § 1.48-3, the used section 38 property the cost of which is to be apportioned to its shareholders.

(3) A shareholder to whom the basis (or cost) of section 38 property is apportioned shall, for purposes of the credit allowed by section 38, be treated as the taxpayer with respect to such property. Thus, the total cost of used section 38 property apportioned to him by the electing small business corporation must be taken into account as cost of used section 38 property in determining whether the \$50,000 limitation on the cost of used section 38 property which may be taken into account by the shareholder in computing qualified investment for any taxable year is exceeded. If a shareholder takes into account in determining his qualified investment any portion of the basis (or cost) of section 38 property placed in service by an electing small

business corporation and if such property subsequently is disposed of or otherwise ceases to be section 38 property in the hands of the corporation, such shareholder shall be subject to the provisions of section 47.

(b) *Summary statement.* An electing small business corporation shall attach to its return a statement showing the apportionment to each shareholder of the total bases of new, and the total cost of used, section 38 properties within each useful life category.

(c) *Example.* This section may be illustrated by the following example:

Example. (1) X Corporation, an electing small business corporation which makes its return on the basis of the calendar year, acquires and places in service on June 1, 1962, three new assets which qualify as new section 38 property and three used

assets which qualify as used section 38 property. The basis of each new, and the cost of each used, section 38 property and the estimated useful life of each property are as follows:

Asset No.	Basis (or cost)	Estimated useful life
1 (new).....	\$30,000	4 years.
2 (new).....	30,000	4 years.
3 (new).....	30,000	8 years.
4 (used).....	12,000	6 years.
5 (used).....	12,000	6 years.
6 (used).....	12,000	8 years.

On December 31, 1962, X Corporation has 10 shares of stock outstanding which are owned as follows: A owns 3 shares, B owns 2 shares, and C owns 5 shares.

(2) Under this section, the total bases of the new, and the total cost of the used, section 38 properties are apportioned to the shareholders of X Corporation as follows:

Useful life category	New—4 to 6 years	New—8 years or more	Used—6 to 8 years	Used—8 years or more
Total bases or total cost.....	\$60,000	\$30,000	\$24,000	\$12,000
Shareholder A (3/10).....	18,000	9,000	7,200	3,600
Shareholder B (2/10).....	12,000	6,000	4,800	2,400
Shareholder C (5/10).....	30,000	15,000	12,000	6,000

Assume that shareholders A, B and C did not place in service during their taxable years in which falls December 31, 1962 (the last day of X Corporation's taxable year) any section 38 property and that such shareholders did not own any interests in other electing small business corporations, partnerships, estates, or trusts. Under section 46(c), the qualified investment of shareholder A is \$23,400, of shareholder B is \$15,600, and of shareholder C is \$39,000, computed as follows:

SHAREHOLDER A

Basis (or cost)	Applicable percentage	Qualified investment
\$18,000 (new).....	33½	\$6,000
\$9,000 (new).....	100	9,000
\$7,200 (used).....	66⅔	4,800
\$3,600 (used).....	100	3,600
Total.....		23,400

SHAREHOLDER B

Basis (or cost)	Applicable percentage	Qualified investment
\$12,000 (new).....	33½	\$4,000
\$6,000 (new).....	100	6,000
\$4,800 (used).....	66⅔	3,200
\$2,400 (used).....	100	2,400
Total.....		15,600

SHAREHOLDER C

Basis (or cost)	Applicable percentage	Qualified investment
\$30,000 (new).....	33½	\$10,000
\$15,000 (new).....	100	15,000
\$12,000 (used).....	66⅔	8,000
\$6,000 (used).....	100	6,000
Total.....		39,000

§ 1.48-6 Estates and trusts.

(a) *In general.* (1) In the case of an estate or trust, the basis of "new section 38 property" and the cost of "used section 38 property" placed in service during the taxable year shall be apportioned among the estate or trust and its beneficiaries on the basis of the income of such estate or trust allocable to each. Section 38 property shall not (by reason

of such apportionment) lose its character as new section 38 property or used section 38 property, as the case may be. The estimated useful life of such property in the hands of a beneficiary shall be deemed to be the estimated useful life of such property in the hands of the estate or trust. The bases of all new section 38 properties which have a useful life falling within a particular useful life category shall be aggregated; likewise, the cost of all used section 38 properties which have a useful life falling within a particular useful life category shall be aggregated. The total bases of new section 38 properties within each useful life category and the total cost of used section 38 properties within each useful life category shall be apportioned separately. The useful life categories are: (i) 4 years or more but less than 6 years; (ii) 6 years or more but less than 8 years; and (iii) 8 years or more. There shall be apportioned to the estate or trust for its taxable year, and to each beneficiary of such estate or trust for his taxable year in which or with which the taxable year of such estate or trust ends, his share (as determined under paragraph (b) of this section) of the total bases of new section 38 properties within each useful life category, and his share of the total cost of used section 38 properties within each useful life category.

(2) The total cost of used section 38 property that may be apportioned among an estate or trust and its beneficiaries for any taxable year of such estate or trust shall not exceed \$50,000. If the total cost of used section 38 property placed in service during the taxable year by the estate or trust exceeds \$50,000, such estate or trust must select, under paragraph (c)(4) of § 1.48-3, the used section 38 property the cost of which is to be apportioned among such estate or trust and its beneficiaries.

(3) A beneficiary to whom the basis (or cost) of section 38 property is apportioned shall, for purposes of the credit

tioned shall, for purposes of the credit allowed by section 38, be treated as the taxpayer with respect to such property. Thus, the total cost of used section 38 property apportioned to him by the estate or trust must be taken into account as cost of used section 38 property in determining whether the \$50,000 limitation on the cost of used property which may be taken into account by the beneficiary in computing qualified investment for any taxable year is exceeded. If a beneficiary takes into account in determining his qualified investment any portion of the basis (or cost) of section 38 property placed in service by an estate or trust and if such property subsequently is disposed of or otherwise ceases to be section 38 property in the hands of the estate or trust, such beneficiary shall be subject to the provisions of section 47.

(4) For purposes of this section, the term "beneficiary" includes heir, legatee, and devisee.

(b) *Share.* A trust's, estate's, or beneficiary's share of the total bases of new section 38 properties, and the total cost of used section 38 properties, within a useful life category shall be—

(1) The total bases of new (or the total cost of used) section 38 properties which have a useful life falling within such useful life category placed in service in the taxable year of the estate or trust, multiplied by

(2) The amount of income allocable to such estate or trust or to such beneficiary for such taxable year, divided by

(3) The sum of the amounts of income allocable to such estate or trust and all its beneficiaries taken into account under subparagraph (2) of this paragraph.

(c) *Limitation based on amount of tax.* Under section 48(f) (3), in the case of an estate or trust the \$25,000 amount specified in section 46(a) (2) (A) and (B), relating to limitation based on amount of tax, shall be reduced for the taxable year to—

(1) \$25,000, multiplied by

(2) The qualified investment with respect to the total bases of new section 38 properties plus the qualified investment

with respect to the total cost of used section 38 properties, apportioned to such estate or trust under paragraph (a) of this section, divided by

(3) The qualified investment with respect to the total bases of all new section 38 properties plus the qualified investment with respect to the total cost of all used section 38 properties, apportioned among such estate or trust and its beneficiaries.

For purposes of subparagraph (3) of this paragraph, cost of used section 38 property shall not be considered as apportioned to any beneficiary to the extent that such cost is not taken into account by such beneficiary in computing qualified investment in used section 38 property.

(d) *Summary statement.* An estate or trust shall attach to its return a statement showing the apportionment to such estate or trust and to each beneficiary of the total bases of new, and the total cost of used, section 38 properties within each useful life category.

(e) *Example.* This section may be illustrated by the following example:

Example. (1) XYZ Trust, which makes its return on the basis of the calendar year, acquires and places in service on June 1, 1962, three new assets which qualify as new section 38 property and three used assets which qualify as used section 38 property. The basis of the new, and the cost of the used, section 38 property and the estimated useful life of each property are as follows:

Asset No.	Basis (or cost)	Estimated useful life
1 (new)	\$30,000	4 years.
2 (new)	30,000	4 years.
3 (new)	30,000	8 years.
4 (used)	12,000	6 years.
5 (used)	12,000	6 years.
6 (used)	12,000	8 years.

For the taxable year 1962 the income of XYZ Trust is \$20,000 which is allocable as follows: \$10,000 to XYZ Trust, \$6,000 to beneficiary A, and \$4,000 to beneficiary B. Beneficiaries A and B make their returns on the basis of a calendar year.

(2) Under this section, the total bases of the new, and the total cost of the used, section 38 properties are apportioned to XYZ Trust and its beneficiaries as follows:

Useful life category	New—4 to 6 years	New—8 years or more	Used—6 to 8 years	Used—8 years or more
Total bases or total cost	\$60,000	\$30,000	\$24,000	\$12,000
XYZ Trust (\$10,000)	30,000	15,000	12,000	6,000
Beneficiary A (\$6,000)	18,000	9,000	7,200	3,600
Beneficiary B (\$4,000)	12,000	6,000	4,800	2,400

Assume that beneficiary A placed in service during his taxable year 1962 new section 38 property with a basis of \$10,000 and an estimated useful life of 8 years. Also, assume that beneficiary B did not place in service during his taxable year 1962 any section 38 property and that beneficiaries A and B did not own any interests in other trusts, estates, partnerships, or electing small business corporations. Under section 46(c), the qualified investment of XYZ Trust is \$39,000, of beneficiary A is \$33,400, and of beneficiary B is \$15,600, computed as follows:

XYZ TRUST			
Basis (or cost)	Applicable percentage	Qualified investment	
\$30,000 (new)	33%	\$10,000	
\$15,000 (new)	100	15,000	
\$12,000 (used)	66%	8,000	
\$6,000 (used)	100	6,000	
Total		39,000	

BENEFICIARY A

\$18,000 (new)	33%	\$6,000
\$9,000 (new)	100	9,000
\$7,200 (used)	66%	4,800
\$8,600 (used)	100	8,600
\$10,000 (new)	100	23,400
Total		33,400

BENEFICIARY B

\$12,000 (new)	33%	\$4,000
\$6,000 (new)	100	6,000
\$4,800 (used)	66%	3,200
\$2,400 (used)	100	2,400
Total		15,600

(4) In the case of XYZ Trust, the \$25,000 amount specified in section 46(a) (2) (A) and (B) is reduced to \$12,500, computed as follows: (i) \$25,000, multiplied by (ii) \$39,000 (qualified investment apportioned to the trust), divided by (iii) \$78,000 (total qualified investment apportioned among such trust (\$39,000), beneficiary A (\$23,400), and beneficiary B (\$15,600)).

§ 1.48-7 Adjustment to basis.

(a) *Reduction of basis; general.*—(1) *In general.* Under section 48(g) (1), the basis of "section 38 property" placed in service before January 1, 1964, shall be reduced by an amount equal to 7 percent of the "qualified investment" with respect to such property. The reduction in basis shall be made as of the time such property is placed in service by the taxpayer. The basis of such property must be reduced by 7 percent of the qualified investment even though the limitation based on amount of tax under section 46(a) (2) reduces the amount of the credit allowed by section 38 for the taxable year in which the property is placed in service. The reduction in basis of section 38 property placed in service before January 1, 1964, shall be taken into account for all purposes of subtitle A of the Code, except in computing (or recomputing in the case of early dispositions, etc.) the qualified investment with respect to such property. Thus, such reduction in basis is taken into account in determining a reasonable allowance for depreciation under section 167, except that the additional amount allowed under section 179 (relating to additional first-year depreciation allowance for small business) with respect to the cost of certain property is determined without regard to such reduction in basis. Section 48(g) (1) and this section do not apply to section 38 property placed in service after December 31, 1963. For increase in basis of property to which this section applies, see section 203(a) (2) (A) of the Revenue Act of 1964 (78 Stat. 33).

(2) *Special rules.* For purposes of applying subparagraph (1) of this paragraph—

(i) If, under § 1.48-4, the lessor of new section 38 property makes a valid election to treat the lessee as having purchased such property for purposes of the credit allowed by section 38, the basis of such property shall not be reduced.

(ii) If property is used section 38 property and if the cost, or any part

thereof, of such property is not, because of the application of the \$50,000 limitation on the cost of used section 38 property, taken into account in computing qualified investment (see paragraph (c) of § 1.48-3) by the person who placed such property in service or by a person to whom the cost of such property was apportioned, no reduction shall be made to the basis of such property to the extent such cost, or any part thereof, is not so taken into account.

(iii) In the case of used section 38 property within a particular useful life category the cost of which is apportioned by an electing small business corporation, estate, or trust, if any part of such cost is not taken into account in computing qualified investment (because of the \$50,000 limitation) by a shareholder or beneficiary, the electing small business corporation, estate, or trust shall choose, to the extent such cost is not so taken into account, the item (or items) of used section 38 property, within such useful life category, with respect to which no reduction in basis shall be made.

(iv) The basis of section 38 property, which is disposed of or otherwise ceases to be section 38 property in the taxable year in which it is placed in service (except where section 47(b) or 46(c)(4) applies), shall not be reduced. See paragraph (a)(2) of § 1.48-3.

(3) *Examples.* This paragraph may be illustrated by the following examples:

Example (1). (i) X Corporation, which makes its return on the basis of the calendar year, acquires and places in service on January 2, 1962, an item of new section 38 property with a basis of \$10,000 and a useful life of 10 years. The amount of qualified investment with respect to such asset is \$10,000 (\$10,000 basis multiplied by 100 percent applicable percentage). For the taxable year 1962, X Corporation is allowed under section 38 a credit of \$700 (7 percent of \$10,000) against its liability for tax of \$1,000.

(ii) Under section 48(g)(1), the basis of the property is reduced to \$9,300 (\$10,000 minus \$700). Thus, for purposes of determining a reasonable allowance for depreciation under section 167 with respect to such property for the taxable year 1962, its adjusted basis is \$9,300.

Example (2). (i) The facts are the same as in example (1) except that for the taxable year 1962 X Corporation's liability for tax under section 48(a)(3) is \$500. Therefore, the credit allowed by section 38 against X Corporation's liability for tax for 1962 is limited to \$500 and the excess of \$200 (\$700 credit earned minus \$500 limitation) is an investment credit carryover.

(ii) The result is the same as in example (1), that is, under section 48(g)(1), the basis of the property is reduced to \$9,300 (\$10,000 minus \$700).

Example (3). (i) The facts are the same as in example (1) except that the property is, for purposes of depreciation, placed in a multiple asset account. On January 1, 1962, the cost or other basis of the property in such account amounted to \$50,000 and no other additions or retirements were reflected in such account during 1962.

(ii) Under section 48(g)(1), since the basis of the property is reduced to \$9,300 (\$10,000 minus \$700), the cost or other basis of the property in the multiple asset account is increased to \$59,300 (\$50,000 plus \$9,300) for purposes of computing depreciation under section 167.

Example (4). (i) The facts are the same as in example (1) except that X Corporation

makes a valid election under paragraph (a) of § 1.179-4 to claim an additional first-year depreciation allowance with respect to the entire cost of the property.

(ii) Under section 48(g)(1), the basis of the property is reduced to \$9,300 (\$10,000 minus \$700). In addition, \$2,000 (20 percent of \$10,000) is allowed as an additional first-year depreciation allowance. Thus, for purposes of determining a reasonable allowance for depreciation under section 167 (in addition to the \$2,000 computed under section 179) for the taxable year 1962 with respect to such property, its adjusted basis is \$7,300 (\$9,300 minus \$2,000).

Example (5). (i) X Corporation acquires and places in service on January 1, 1962, used assets Nos. 1, 2, and 3. Each asset has a cost of \$25,000 and a useful life of 10 years. Such used assets qualify as used section 38 property. X Corporation selects the \$25,000 cost of used asset No. 1 and the \$25,000 cost of used asset No. 2 to be taken into account in computing qualified investment.

(ii) Under section 48(g)(1), the basis of asset No. 1 is reduced to \$23,250, that is, basis of \$25,000 minus \$1,750 (7 percent of \$25,000 qualified investment). Likewise, the basis of asset No. 2 is reduced to \$23,250. The basis of asset No. 3 is not reduced.

Example (6). (i) X Corporation acquires and places in service on January 1, 1962, used assets Nos. 1, 2, and 3 which qualify as used section 38 property. Each asset has a cost of \$20,000 and a useful life of 10 years. X Corporation selects the \$20,000 cost of used asset No. 1, the \$20,000 cost of used asset No. 2, and \$10,000 of the cost of used asset No. 3 to be taken into account in computing qualified investment.

(ii) Under section 48(g)(1), the basis of asset No. 1 is reduced to \$18,600, that is, basis of \$20,000 minus \$1,400 (7 percent of \$20,000 qualified investment). Likewise, the basis of asset No. 2 is reduced to \$18,600. The basis of asset No. 3 is reduced to \$19,300, that is basis of \$20,000 minus \$700 (7 percent of \$10,000 qualified investment).

Example (7). (i) X Corporation, an electing small business corporation which makes its return on the basis of the calendar year, acquires and places in service on January 1, 1962, five used assets which qualify as used section 38 property. The cost of each used section 38 property and the estimated useful life of each property are as follows:

Asset No.	Cost	Estimated useful life
1.....	\$20,000	8 years.
2.....	24,000	6 years.
3.....	3,000	4 years.
4.....	6,000	4 years.
5.....	3,000	4 years.

On December 31, 1962, X Corporation has 10 shares of stock outstanding which are owned as follows: A owns 3 shares, B owns 2 shares, and C owns 5 shares. All the shareholders make their returns on the basis of a calendar year. X Corporation selects the \$20,000 cost of asset No. 1, the \$24,000 cost of asset No. 2, the \$3,000 cost of asset No. 3, and \$3,000 of the cost of asset No. 4 to be apportioned to its shareholders. Under § 1.48-5, the total cost of the used section 38 property selected is apportioned to the shareholders of X Corporation as follows:

Useful life category	Used—4 to 6 years	Used—6 to 8 years	Used—8 years or more
Total cost.....	\$6,000	\$24,000	\$20,000
Shareholder A (3/10).....	1,800	7,200	6,000
Shareholder B (2/10).....	1,200	4,800	4,000
Shareholder C (5/10).....	3,000	12,000	10,000

Assume that shareholders A, B, and C did not place in service during their taxable years ending December 31, 1962, any section 38 property and that such shareholders did not own any interests in other electing small business corporations, partnerships, estates, or trusts. Under section 46(c)(1)(B) each shareholder computes his qualified investment as follows:

SHAREHOLDER A		
Cost	Applicable percentage	Qualified investment
\$1,800.....	33 1/3%	\$600
\$7,200.....	66 2/3%	4,800
\$6,000.....	100	6,000
		11,400

SHAREHOLDER B		
Cost	Applicable percentage	Qualified investment
\$1,200.....	33 1/3%	\$400
\$4,800.....	66 2/3%	3,200
\$4,000.....	100	4,000
		7,600

SHAREHOLDER C		
Cost	Applicable percentage	Qualified investment
\$3,000.....	33 1/3%	\$1,000
\$12,000.....	66 2/3%	8,000
\$10,000.....	100	10,000
		19,000

(ii) Under section 48(g)(1), the basis of each asset (except asset No. 5) is reduced by 7 percent of the qualified investment with respect to such asset, as follows:

Asset No.	Basis before reduction	Qualified investment	Basis after reduction
1.....	\$20,000	Minus 7% of \$20,000.....	\$18,600
2.....	24,000	Minus 7% of \$16,000.....	22,880
3.....	3,000	Minus 7% of \$1,000.....	2,930
4.....	6,000	Minus 7% of \$1,000.....	5,930

The basis of asset No. 5 is not reduced.

Example (8). (i) The facts are the same as in example (7) except that shareholder C acquired and placed in service on June 1, 1962, in his individual proprietorship, used asset No. 6 with a cost of \$27,000 and an estimated useful life of 10 years. In computing his qualified investment, shareholder C selects the \$27,000 cost of asset No. 6, the \$10,000 cost of used section 38 property within the 8 years or more useful life category apportioned to him by X Corporation, the \$12,000 cost of used section 38 property within the 6 to 8 years useful life category apportioned to him by X Corporation, and \$1,000 of the cost of used section 38 property within the 4 to 6 years useful life category apportioned to him by X Corporation. Under section 46(c)(1)(B), he computes his qualified investment as follows:

Proprietorship	Cost	Applicable percentage	Qualified investment
Asset No. 6.....	\$27,000	100	\$27,000
Apportioned by X Corporation:			
8 years or more.....	10,000	100	10,000
6 to 8 years.....	12,000	66 2/3%	8,000
4 to 6 years.....	1,000	33 1/3%	333
			45,333

(ii) Since only \$4,000 of the \$6,000 cost of used section 38 property in the 4 to 6 years useful life category apportioned to X Corporation was taken into account by share-

holders A, B, and C in computing their qualified investment, only \$4,000 of the bases of the assets in such category is subject to reduction. Under subparagraph (2)(iii) of this paragraph, X must choose an item of property in such category, \$2,000 of the basis of which will not be subject to the reduction. Therefore, X Corporation chooses to reduce the basis of asset No. 4 by 7 percent of qualified investment with respect to only \$1,000 of the cost of such asset (in lieu of the \$3,000 previously selected). The bases of assets Nos. 1, 2, and 3 are reduced by 7 percent of the qualified investment with respect to each such asset. The basis of each asset is reduced as follows:

Asset No.	Basis before reduction	Qualified investment	Basis after reduction
1.....	\$20,000	Minus 7% of \$20,000.....	\$18,600
2.....	24,000	Minus 7% of \$16,000.....	22,880
3.....	3,000	Minus 7% of \$1,000.....	2,830
4.....	6,000	Minus 7% of \$333.....	5,977

The basis of asset No. 5 is not reduced.

(iii) The basis of asset No. 6, in the hands of shareholder C, is reduced to \$25,110, that is, basis of \$27,000 minus \$1,890 (7 percent of \$27,000 qualified investment).

Asset No.	Estimated useful life	Cost	Partner's share of cost		
			A (50%)	B (30%)	C (20%)
1.....	8 years.....	\$20,000	\$10,000	\$6,000	\$4,000
2.....	6 years.....	24,000	12,000	7,200	4,800
3.....	4 years.....	3,000	1,500	900	600
4.....	4 years.....	3,000	1,500	900	600

Each partner makes his return on the basis of the calendar year. Assume that partners A, B, and C did not place in service during their taxable years ending December 31, 1962, any section 38 property and that such partners did not own any interests in other partnerships, estates, trusts, or electing small business corporations. Under section 46(c), each partner computes his qualified investment as follows:

PARTNER A			
Asset No.	Share of cost	Applicable percentage	Qualified investment
1.....	\$10,000	100	\$10,000
2.....	12,000	66⅔	8,000
3.....	1,500	33⅓	500
4.....	1,500	33⅓	500
			19,000

PARTNER B			
Asset No.	Share of cost	Applicable percentage	Qualified investment
1.....	\$6,000	100	\$6,000
2.....	7,200	66⅔	4,800
3.....	900	33⅓	300
4.....	900	33⅓	300
			11,400

PARTNER C			
Asset No.	Share of cost	Applicable percentage	Qualified investment
1.....	\$4,000	100	\$4,000
2.....	4,800	66⅔	3,200
3.....	600	33⅓	200
4.....	600	33⅓	200
			7,600

(ii) Under section 48(g)(1), the basis of each asset selected by the partnership is reduced by 7 percent of the qualified investment with respect to such asset, as follows:

Example (9). (i) ABC Partnership, which makes its return on the basis of the calendar year, acquires and places in service on January 1, 1962, five used assets which qualify as used section 38 property. The cost of each used section 38 property and the estimated useful life of each property are as follows:

Asset No.	Cost	Estimated useful life
1.....	\$20,000	8 years.
2.....	24,000	6 years.
3.....	3,000	4 years.
4.....	6,000	4 years.
5.....	3,000	4 years.

Partners A, B, and C share the profits and the losses of partnership ABC in the ratio of 50 percent, 30 percent, and 20 percent, respectively. ABC Partnership selects the \$20,000 cost of asset No. 1, the \$24,000 cost of asset No. 2, the \$3,000 cost of asset No. 3, and \$3,000 of the cost of asset No. 4, to be taken into account by its members in computing qualified investment. Under paragraph (f)(2) of § 1.46-3, each partner's share of the cost of the partnership used section 38 property to be taken into account in computing qualified investment is as follows:

Asset No.	Basis before reduction	Qualified investment	Basis after reduction
1.....	\$20,000	Minus 7% of \$20,000.....	\$18,600
2.....	24,000	Minus 7% of \$16,000.....	22,880
3.....	3,000	Minus 7% of \$1,000.....	2,830
4.....	6,000	Minus 7% of \$1,000.....	5,930

The basis of asset No. 5 is not reduced.

Example (10). (i) The facts are the same as in example (9) except that partner A acquired and placed in service on June 1, 1962, in his individual proprietorship, used asset No. 6 with a cost of \$26,000 and an estimated useful life of 10 years. Partner A selects the \$26,000 cost of asset No. 6, his \$10,000 share of the cost of asset No. 1, his \$12,000 share of the cost of asset No. 2, his \$1,500 share of the cost of asset No. 3, and \$500 of his share of the cost of asset No. 4, to be taken into account in computing his qualified investment. Under section 46(c), he computes his qualified investment as follows:

Proprietorship property	Cost	Applicable percentage	Qualified investment
Asset No. 6.....	\$26,000	100	\$26,000
Partnership property			
Asset No.	Share of cost	Applicable percentage	Qualified investment
Asset No. 1.....	\$10,000	100	10,000
Asset No. 2.....	12,000	66⅔	8,000
Asset No. 3.....	1,500	33⅓	500
Asset No. 4.....	500	33⅓	167
			44,667

(ii) Under section 48(g)(1), the basis of each asset selected by the partnership is reduced by 7 percent of the qualified investment with respect to such asset as follows:

Asset No.	Basis before reduction	Qualified investment	Basis after reduction
1.....	\$20,000	Minus 7% of \$20,000.....	\$18,600
2.....	24,000	Minus 7% of \$16,000.....	22,880
3.....	3,000	Minus 7% of \$1,000.....	2,830
4.....	6,000	Minus 7% of \$667.....	5,933

The basis of asset No. 5 is not reduced.

(iii) The basis of asset No. 6, in the hands of partner A, is reduced to \$24,180, that is, basis of \$26,000 minus \$1,820 (7 percent of \$26,000 qualified investment).

(b) *Reduction of basis; purchase of leased property by lessee treated as purchaser.* (1) If a lessor of property placed in service before January 1, 1964, makes a valid election under § 1.48-4 to treat the lessee as having purchased such property for purposes of the credit allowed by section 38 and if such lessee at a later date (in a taxable year of the lessee beginning before January 1, 1964) actually purchases such property, the basis of such property shall be reduced, as of the time of the actual purchase, by an amount equal to the excess of—

(i) The credit earned (as defined in paragraph (k)(2)(i) of § 1.48-4) with respect to such property, over

(ii) The sum of the amounts by which the lessee-purchaser has decreased, under paragraph (k)(2) of § 1.48-4, his deductions otherwise allowable under section 162 for amounts paid or accrued to the lessor-vendor under the lease with respect to such property.

(2) The operation of this paragraph may be illustrated by the following example:

Example. (i) X Corporation acquires on January 1, 1962, an item of new section 38 property with a basis of \$12,000 and with a useful life of 8 years. Y Corporation, which makes its return on the basis of a calendar year, leases such property from X Corporation and places it in service on February 1, 1962. Under § 1.48-4, X Corporation makes a valid election to treat Y Corporation as having purchased such property for purposes of the credit allowed by section 38. Under paragraph (k)(2)(i) of § 1.48-4, the amount of the credit earned with respect to such property is \$840 (7 percent of \$12,000). For the taxable year 1962 Y Corporation decreases, under paragraph (k)(2)(ii) of § 1.48-4, its deductions otherwise allowable under section 162 for amounts paid to X Corporation under the lease with respect to such property by \$96.25 (\$840 multiplied by 11/96). On January 1, 1963, Y Corporation actually purchases such property from X Corporation for \$9,000.

(ii) As of January 1, 1963, Y Corporation must reduce the basis of the property by \$743.75 (\$840 minus \$96.25). Thus, for purposes of determining a reasonable allowance for depreciation under section 167 with respect to such property for the taxable year 1963, its adjusted basis is \$8,256.25 (\$9,000 minus \$743.75).

[F.R. Doc. 64-4647; Filed, May 7, 1964; 8:50 a.m.]

SUBCHAPTER F—PROCEDURE AND
ADMINISTRATION

[T.D. 6730]

PART 301—PROCEDURE AND
ADMINISTRATION

Periods of Limitations and Interest

In order to conform the Regulations on Procedure and Administration (26 CFR Part 301) to the amendments made to the Internal Revenue Code of 1954 by the Federal-Aid Highway Act of 1961 (75 Stat. 122), the Trade Expansion Act of 1962 (76 Stat. 872), the Revenue Act of 1962 (76 Stat. 960), and the Act of October 23, 1962 (Public Law 87-858, 76 Stat. 1134), the regulations are amended as follows:

PARAGRAPH 1. Section 301.6501(c) is amended by revising subsection (c) (6) of section 6501 and the historical note to read as follows:

§ 301.6501(c) Statutory provisions; limitations on assessment and collection; exceptions.

Sec. 6501. *Limitations on assessment and collection.* . . .

(c) *Exceptions.* . . .
(6) *Tax resulting from certain distributions or from termination as life insurance company.* In the case of any tax imposed under section 802(a) by reason of section 802(b) (3) on account of a termination of the taxpayer as an insurance company or as a life insurance company to which section 815 (d) (2) (A) applies, or on account of a distribution by the taxpayer to which section 815(d) (2) (B) applies, such tax may be assessed within 3 years after the return was filed (whether or not such return was filed on or after the date prescribed) for the taxable year for which the taxpayer ceases to be an insurance company, the second taxable year for which the taxpayer is not a life insurance company, or the taxable year in which the distribution is actually made, as the case may be.

[Sec. 6501(c) as amended by sec. 3(g), Life Insurance Company Income Tax Act 1959 (73 Stat. 140); sec. 3(b) (4), Act of Oct. 23, 1962 (Pub. Law 87-858, 76 Stat. 1137)]

PAR. 2. Section 301.6501(h) is amended by revising subsection (h) of section 6501 and the historical note to read as follows:

§ 301.6501(h) Statutory provisions; limitations on assessment and collection; net operating loss carrybacks.

Sec. 6501. *Limitations on assessment and collection.* . . .

(h) *Net operating loss carrybacks.* In the case of a deficiency attributable to the application to the taxpayer of a net operating loss carryback (including deficiencies which may be assessed pursuant to the provisions of section 6213(b) (2)), such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the net operating loss which results in such carryback may be assessed, or within 18 months after the date on which the taxpayer files in accordance with section 172(b) (3) a copy of the certification (with respect to such taxable year) issued under section 317 of the Trade Expansion Act of 1962, whichever is later.

[Sec. 6501(h) as added by sec. 81(b), Technical Amendments Act 1958 (72 Stat. 1663); and as amended by sec. 317(c), Trade Expansion Act 1962 (76 Stat. 890)]

PAR. 3. Section 301.6501(h)-1 is amended to read as follows:

§ 301.6501(h)-1 Net operating loss carrybacks.

In the case of a deficiency attributable to the application to the taxpayer of a net operating loss carryback (including deficiencies which may be assessed pursuant to the provisions of section 6213 (b) (2)), such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the net operating loss which results in such carryback may be assessed, or within 18 months after the date on which the taxpayer files in accordance with section 172(b) (3) a copy of the certification (with respect to such taxable year) issued under section 317 of the Trade Expansion Act of 1962, whichever is later.

PAR. 4. Section 301.6501(j), as amended by Treasury Decision 6555, approved March 9, 1961, is redesignated § 301.6501 (k), subsection (j) of section 6501 is redesignated subsection (k), and the historical note is revised. The amended provisions read as follows:

§ 301.6501(k) Statutory provisions; limitations on assessment and collection; joint income return after separate return.

Sec. 6501. *Limitations on assessment and collection.* . . .

(k) *Joint income return after separate return.* For period of limitations for assessment and collection in the case of a joint income return filed after separate returns have been filed, see section 6013(b) (3) and (4).

[Sec. 6501(h) as redesignated by sec. 81(b), Technical Amendments Act 1958 (72 Stat. 1663); sec. 3(c), Act of Sept. 14, 1960 (Pub. Law 86-780, 74 Stat. 1013); sec. 2(e) (1), Revenue Act 1962 (76 Stat. 971)]

PAR. 5. Immediately after § 301.6501 (i)-1 there are inserted the following new sections:

§ 301.6501(j) Statutory provisions; limitations on assessment and collection; investment credit carrybacks.

Sec. 6501. *Limitations on assessment and collection.* . . .

(j) *Investment credit carrybacks.* In the case of a deficiency attributable to the application to the taxpayer of an investment credit carryback, such deficiency may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the unused investment credit which results in such carryback may be assessed.

[Sec. 6501(j) as added by sec. 2(e) (1), Revenue Act 1962 (76 Stat. 971)]

§ 301.6501(j)-1 Investment credit carryback; taxable years ending after December 31, 1961.

With respect to taxable years ending after December 31, 1961, a deficiency attributable to the application to the taxpayer of an investment credit carryback may be assessed at any time before the expiration of the period within which a deficiency for the taxable year of the unused investment credit which results in such carryback may be assessed.

PAR. 6. Section 301.6511(d) is amended by revising subsection (d) (2) (A) of section 6511 and the historical note, and by adding a new paragraph (4) to section

6511(d). The amended provisions read as follows:

§ 301.6511(d) Statutory provisions; limitations on credit or refund; special rules applicable to income taxes.

Sec. 6511. *Limitations on credit or refund.* . . .

(d) *Special rules applicable to income taxes.* . . .

(2) *Special period of limitation with respect to net operating loss carrybacks—(A) Period of limitation.* If the claim for credit or refund relates to an overpayment attributable to a net operating loss carryback, in lieu of the 3-year period of limitation prescribed in subsection (a), the period shall be that period which ends with the expiration of the 15th day of the 40th month (or the 39th month in the case of a corporation) following the end of the taxable year of the net operating loss which results in such carryback, or the period prescribed in subsection (c) in respect of such taxable year, whichever expires later; except that—

(i) With respect to an overpayment attributable to a net operating loss carryback to any year on account of a certification issued to the taxpayer under section 317 of the Trade Expansion Act of 1962, the period shall not expire before the expiration of the sixth month following the month in which such certification is issued to the taxpayer, and

(ii) With respect to an overpayment attributable to the creation of, or an increase in, a net operating loss carryback as a result of the elimination of excessive profits by a renegotiation (as defined in section 1481(a) (1) (A)), the period shall not expire before September 1, 1959, or the expiration of the twelfth month following the month in which the agreement or order for the elimination of such excessive profits becomes final, whichever is the later.

In the case of such a claim, the amount of the credit or refund may exceed the portion of the tax paid within the period provided in subsection (b) (2) or (c), whichever is applicable, to the extent of the amount of the overpayment attributable to such carryback.

(4) *Special period of limitation with respect to investment credit carrybacks—(A) Period of limitation.* If the claim for credit or refund relates to an overpayment attributable to an investment credit carryback, in lieu of the 3-year period of limitation prescribed in subsection (a), the period shall be that period which ends with the expiration of the 15th day of the 40th month (or 39th month, in the case of a corporation) following the end of the taxable year of the unused investment credit which results in such carryback, or the period prescribed in subsection (c) in respect of such taxable year, whichever expires later. In the case of such a claim, the amount of the credit or refund may exceed the portion of the tax paid within the period provided in subsection (b) (2) or (c), whichever is applicable, to the extent of the amount of the overpayment attributable to such carryback.

(B) *Applicable rules.* If the allowance of a credit or refund of an overpayment of tax attributable to an investment credit carryback is otherwise prevented by the operation of any law or rule of law other than section 7122, relating to compromises, such credit or refund may be allowed or made, if claim therefor is filed within the period provided in subparagraph (A) of this paragraph. In the case of any such claim for credit or refund, the determination by any court, including the Tax Court, in any proceeding in which the decision of the court has become final, shall not be conclusive with respect to the investment credit, and the effect of such credit, to the extent that such credit is affected by a carryback which was not in issue in such proceeding.

[Sec. 6511(d) as amended by sec. 82(d), Technical Amendments Act 1958 (72 Stat. 1663); sec. 1(a), Act of Sept. 16, 1959 (Pub. Law 86-280, 73 Stat. 563); sec. 317(d), Trade Expansion Act 1962 (76 Stat. 891); sec. 2(e) (2), Revenue Act 1962 (76 Stat. 971)]

PAR. 7. Section 301.6511(d)-2 is amended by revising subparagraph (1) of paragraph (a) to read as follows:

§ 301.6511(d)-2 Overpayment of income tax on account of net operating loss carryback.

(a) *Special period of limitation.* (1) If the claim for credit or refund relates to an overpayment of income tax attributable to a net operating loss carryback, provided in section 172(b), then in lieu of the 3-year period from the time the return was filed in which the claim may be filed or credit or refund allowed, as prescribed in section 6511 (a) or (b), the period shall be whichever of the following 2 periods expires later:

(i) The period which ends with the expiration of the fifteenth day of the fortieth month (or thirty-ninth month, in the case of a corporation) following the end of the taxable year of the net operating loss which resulted in the carryback; or

(ii) The period which ends with the expiration of the period prescribed in section 6511(c) within which a claim for credit or refund may be filed with respect to the taxable year of the net operating loss which resulted in the carryback;

except that—

(a) With respect to an overpayment attributable to a net operating loss carryback to any year on account of a certification issued to the taxpayer under section 317 of the Trade Expansion Act of 1962, the period shall not expire before the expiration of the sixth month following the month in which such certification is issued to the taxpayer, and

(b) With respect to an overpayment attributable to the creation of, or an increase in, a net operating loss carryback as a result of the elimination of excessive profits by a renegotiation (as defined in section 1481(a) (1) (A)), the period shall not expire before September 1, 1959, or the expiration of the twelfth month following the month in which the agreement or order for the elimination of such excessive profits becomes final, whichever is the later.

PAR. 8. Immediately after § 301.6511 (d)-3 there is inserted the following new section:

§ 301.6511(d)-4 Overpayment of income tax on account of investment credit carryback.

(a) *Special period of limitation.* (1) If the claim for credit or refund relates to an overpayment of income tax attributable to an investment credit carryback, provided in section 46(b), then in lieu of the 3-year period from the time the return was filed in which the claim may be filed or credit or refund allowed, as prescribed in section 6511 (a) or (b), the period shall be whichever of the following 2 periods expires later:

(i) The period which ends with the expiration of the fifteenth day of the fortieth month (or thirty-ninth month, in the case of a corporation) following the end of the taxable year of the unused investment credit which resulted in the carryback; or

(ii) The period which ends with the expiration of the period prescribed in section 6511(c) within which a claim for credit or refund may be filed with respect to the taxable year of the unused investment credit which resulted in the carryback.

(2) In the case of a claim for credit or refund involving an investment credit carryback described in subparagraph (1) of this paragraph, the amount of the credit or refund may exceed the portion of the tax paid within the period provided in section 6511 (b) (2) or (c), whichever is applicable, to the extent of the amount of the overpayment attributable to the carryback. If the claim involves an overpayment based not only on an investment credit carryback described in subparagraph (1) of this paragraph but based also on other items, the credit or refund cannot exceed the sum of the following:

(i) The amount of the overpayment which is attributable to the investment credit carryback, and

(ii) The balance of such overpayment up to a limit of the portion, if any, of the tax paid within the period provided in section 6511 (b) (2) or (c), or within the period provided in any other applicable provision of law.

(3) If the claim involves an overpayment based not only on an investment credit carryback described in subparagraph (1) of this paragraph but based also on other items, and if the claim with respect to any items is barred by the expiration of any applicable period of limitation, the portion of the overpayment attributable to the items not so barred shall be determined by treating the allowance of such items as the first adjustment to be made in computing such overpayment. If a claim for credit or refund is not filed, and if credit or refund is not allowed, within the period prescribed in this paragraph, then credit or refund may be allowed or made only if claim therefor is filed, or if such credit or refund is allowed, within the period prescribed in section 6511 (a), (b), or (c), whichever is applicable, subject to the provisions thereof limiting the amount of credit or refund in the case of a claim filed, or if no claim was filed, in case of credit or refund allowed, within such applicable period. For the limitations on the allowance of interest for an overpayment where credit or refund is subject to the provisions of this section, see section 6611 (f).

(b) *Barred overpayments.* If the allowance of a credit or refund of an overpayment of tax attributable to an investment credit carryback is otherwise prevented by the operation of any law or rule of law (other than section 7122, relating to compromises), such credit or refund may be allowed or made under the provisions of section 6511(d) (4) (B) if a claim therefor is filed within the period provided by section 6511(d) (4) (A) and paragraph (a) of this section

for filing a claim for credit or refund of an overpayment attributable to a carryback. In the case of a claim for credit or refund of an overpayment attributable to a carryback, the determination of any court, including the Tax Court, in any proceeding in which the decision of the court has become final, shall not be conclusive with respect to the investment credit, and the effect of such credit, to the extent that such credit is affected by a carryback which was not in issue in such proceeding.

PAR. 9. Section 301.6601 is amended by revising subsections (c) (2) and (e) of section 6601 and the historical note to read as follows:

§ 301.6601 Statutory provisions; interest on underpayment, nonpayment, or extensions of time for payment, of tax.

Sec. 6601. *Interest on underpayment, nonpayment, or extensions of time for payment, of tax.* * * *

(c) *Last date prescribed for payment.* * * *

(2) *Installment payments.* In the case of an election under section 6152 (a) or 6156 (a) to pay the tax in installments—

(A) The date prescribed for payment of each installment of the tax shown on the return shall be determined under section 6152(b) or 6156(b), as the case may be, and

(B) The last date prescribed for payment of the first installment shall be deemed the last date prescribed for payment of any portion of the tax not shown on the return.

(e) *Income tax reduced by carryback—*

(1) *Net operating loss carryback.* If the amount of any tax imposed by subtitle A is reduced by reason of a carryback of a net operating loss, such reduction in tax shall not affect the computation of interest under this section for the period ending with the last day of the taxable year in which the net operating loss arises.

(2) *Investment credit carryback.* If the credit allowed by section 38 for any taxable year is increased by reason of an investment credit carryback, such increase shall not affect the computation of interest under this section for the period ending with the last day of the taxable year in which the investment credit carryback arises.

[Sec. 6601 as amended by secs. 66(c), 83(a) (1), 84(a), Technical Amendments Act 1958 (72 Stat. 1658, 1663, 1664); sec. 206 (e), Small Business Tax Revision Act 1958 (72 Stat. 1685); sec. 203(c) (2), Federal-Aid Highway Act 1961 (75 Stat. 126); sec. 2(e) (3), Revenue Act 1962 (76 Stat. 972)]

PAR. 10. Section 301.6601-1, as amended by Treasury Decision 6585, approved December 21, 1961, is further amended by revising paragraphs (c) (2) (i) and (e) to read as follows:

§ 301.6601-1 Interest on underpayments.

(c) *Last date prescribed for payment.* * * *

(2) (i) If a tax or portion thereof is payable in installments in accordance with an election made under section 6152(a) or 6156(a), the last date prescribed for payment of any installment of such tax or portion thereof shall be determined under the provisions of section 6152(b) or 6156(b), as the case may be, and interest shall run on any unpaid

installment from such last date to the date on which payment is received. However, in the event installment privileges are terminated for failure to pay an installment when due as provided by section 6152(d) and the time for the payment of any remaining installment is accelerated by the issuance of a notice and demand therefor, interest shall run on such unpaid installment from the date of the notice and demand to the date on which payment is received. But see section 6601(f) (4).

(e) *Income tax reduced by carryback.*

(1) The carryback of a net operating loss or an investment credit shall not affect the computation of interest on any income tax for the period commencing with the last date prescribed for the payment of such tax and ending with the last day of the taxable year in which the loss or credit arises. For example, if the carryback of a net operating loss or an investment credit to a prior taxable period eliminates or reduces a deficiency in income tax for that period, the full amount of the deficiency will nevertheless bear interest at the rate of 6 percent per annum from the last date prescribed for payment of such tax until the last day of the taxable year in which the loss or credit arose. Interest will continue to run beyond such last day on any portion of the deficiency which is not eliminated by the carryback.

(2) Where an extension of time for payment of income tax has been granted under section 6164 to a corporation expecting a net operating loss carryback, interest is payable at the rate of 6 percent per annum on the amount of such unpaid tax from the last date prescribed for payment thereof without regard to such extension.

(3) Where there has been an allowance of an overpayment attributable to a net operating loss carryback or an investment credit carryback and all or part of such allowance is later determined to be excessive, interest shall be computed on the excessive amount from the last day of the year in which the net operating loss or investment credit arose until the date on which the repayment of such excessive amount is received.

PAR. 11. Section 301.6611 is amended by revising subsection (f) of section 6611 and the historical note to read as follows:

§ 301.6611 Statutory provisions; interest on overpayments.

Sec. 6611. *Interest on overpayments.* * * *

(1) *Refund of income tax caused by carryback.*—(1) *Net operating loss carryback.* For purposes of subsection (a), if any overpayment of tax imposed by subtitle A results from a carryback of a net operating loss, such overpayment shall be deemed not to have been made prior to the close of the taxable year in which such net operating loss arises.

(2) *Investment credit carryback.* For purposes of subsection (a), if any overpayment of tax imposed by subtitle A results from an investment credit carryback, such overpayment shall be deemed not to have been made prior to the close of the taxable year in which such investment credit carryback arises.

[Sec. 6611 as amended by secs. 42(b), 83 (b), (c), Technical Amendments Act 1958 (72 Stat. 1640, 1664); sec. 2(e)(4), Revenue Act 1962 (76 Stat. 972)]

PAR. 12. Section 301.6611-1, as amended by Treasury Decision 6585, approved December 21, 1961, is further amended by revising paragraph (c) to read as follows:

§ 301.6611-1 Interest on overpayments.

(c) *Refund of income tax caused by carryback.* If any overpayment of tax imposed by subtitle A of the Code results from the carryback of a net operating loss or an investment credit, such overpayment, for purposes of this section, shall be deemed not to have been made prior to the end of the taxable year in which the loss or credit arises.

Because this Treasury decision makes only technical changes, it is hereby found that it is unnecessary to issue this Treasury decision with notice and public procedure thereon under section 4(a) of the Administrative Procedure Act, approved June 11, 1946, or subject to the effective date limitation of section 4(c) of that Act.

(Sec. 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805))

MORTIMER M. CAPLIN,
Commissioner of Internal Revenue.

Approved: May 5, 1964.

STANLEY S. SURREY,
Assistant Secretary of the
Treasury.

[F.R. Doc. 64-4648; Filed, May 7, 1964;
8:50 a.m.]

Title 29—LABOR

Chapter XIII—Bureau of Labor Standards, Department of Labor

PART 1501—SAFETY AND HEALTH REGULATIONS FOR SHIP REPAIRING

PART 1502—SAFETY AND HEALTH REGULATIONS FOR SHIPBUILDING

PART 1503—SAFETY AND HEALTH REGULATIONS FOR SHIPBREAKING

Fire Prevention; Correction

In the documents revising 29 CFR Parts 1501 and 1502 and establishing 29 CFR Part 1503 published in the FEDERAL REGISTER on March 27, 1964 (29 F.R. 4001, 4027 and 4051), the following correction is hereby made in matter concerning fire prevention:

The word "enclosed" in the second sentence of 29 CFR 1501.32(g), 1502.32(g), and 1503.32(a)(4) is changed to read "confined".

Because this change involves only a minor correction in language, and results in relief from the stringency of the regulations, notice of proposed rule making, public participation in its adoption, and additional delay in effective date are found to be unnecessary. Accordingly, good cause is found to and I do hereby make the change effective on April 26,

1964, the effective date of the regulation changed.

Signed at Washington, D.C., this 4th day of May 1964.

W. WILLARD WIRTZ,
Secretary of Labor.

[F.R. Doc. 64-4622; Filed, May 7, 1964;
8:47 a.m.]

Title 39—POSTAL SERVICE

Chapter I—Post Office Department MISCELLANEOUS AMENDMENTS TO CHAPTER

The regulations of the Post Office Department are amended as follows:

PART 43—MAIL DEPOSIT AND COLLECTION

I. In § 43.6 subparagraph (1) of paragraph (h), as amended by 28 F.R. 11506, is further amended to show that all inquiries from prospective manufacturers of mailing chutes and receiving boxes shall be referred to the Director, Delivery Services Branch, Bureau of Operations. As so amended, subparagraph (1) reads as follows:

§ 43.6 Mail chutes and receiving boxes.

(h) *Mailing chute and receiving box manufactures.* (1) A firm interested in the manufacture of mailing chutes or mailing chute receiving boxes must submit to the Director, Delivery Services Branch, Bureau of Operations, specifications, drawings, and a full size working model of the chute and receiving box. The chute section should be at least 5 feet in length and must contain a mail slot. This section is to be attached to the receiving box. If the specifications, drawings, and model are found satisfactory, the Director, Delivery Services Branch, Bureau of Operations will request the firm to submit a \$10,000 bond as specified in paragraph (f) (3) of this section. After the bond is examined and approved, he will authorize installation of not more than three mailing chutes and receiving boxes for a 90-day actual service condition test. If no unsatisfactory condition is disclosed during the test period, the Director, Delivery Services Branch, Bureau of Operations, will give the concern final approval for the manufacture of this equipment. The company's name and address will then be added to the list of authorized manufacturers of mailing chutes and receiving boxes.

NOTE: The corresponding Postal Manual section is 153.681.

PART 151—CUSTOMS

II. In 151.5 *Treatment at delivery office*, paragraph (d), as amended by 28 F.R. 4252, is further amended by revising that part of subparagraph (4) which precedes subdivision (i) to show the exemptions regarding customs and or internal revenue taxes for packages addressed to persons entitled to tourist

exemptions. As so revised, that part of subparagraph (4) reads as follows:

§ 151.5 Treatment at delivery office.

(d) *Delivery of dutiable mail.* * * *
(4) A package containing items purchased by the addressee while traveling abroad is usually entitled to free entry under his personal tourist exemption. Articles ordinarily liable for internal-revenue taxes by reason of their importation are free of such taxes if they are free of duty under a tourist exemption. The following conditions apply to packages of this nature assessed with duty and/or revenue tax (hereinafter referred to simply as duty) received at delivery offices:

NOTE: The corresponding Postal Manual section is 261.544.

PART 162—IDEMNITY CLAIMS AND PAYMENTS

III. In § 162.2 *Indemnity payments* delete paragraph (c) (4); and redesignate subparagraph (4) of paragraph (a) as subparagraph (5) and insert a new subparagraph (4) to read as follows:

§ 162.2 Indemnity payments.

(a) *Registered postal union articles.* * * *

(4) *Australia.* Indemnity may be paid in any amount claimed not exceeding \$8.17 for loss (contents and wrapper), regardless of value; and, on the basis of actual value, irrespective of country responsible, for rifling of an article in a registered packet, but not exceeding \$8.17. If United States responsibility, payment may also be made for damage, but not exceeding \$8.17.

NOTE: The corresponding Postal Manual sections are 272.21 d and e.

PART 168—DIRECTORY OF INTERNATIONAL MAIL

IV. In § 168.5 *Individual country regulations* make the following changes:

A. In country "Argentina" under Parcel Post, add the following paragraph to the item *Observations*:

Used clothing addressed to individuals is limited to 22 pounds per parcel. Each parcel containing used clothing must have enclosed a notarized and legalized statement from a dry-cleaning or disinfecting establishment that the clothing has been thoroughly cleaned or disinfected. After the statement has been notarized, the notarization must be certified by the county clerk or other competent official. The statement must then be sent to an Argentine consulate accompanied by a fee of \$7.40 for legalization. After the consulate returns the legalized statement, it must be enclosed in the parcel with the clothing. The wrapper of the parcel must be marked

"Legalized disinfection certificate enclosed."

B. In country "Bahamas," delete the item *Prohibitions* under Postal Union mail; and under Parcel Post, amend the first paragraph of the item *Insurance* to read as follows:

Insurance. The following insurance fees and limits of indemnity apply:

Limit of indemnity:	Fee, cents
Not over \$10.....	20
From \$10.01 to \$25.....	25
From \$25.01 to \$50.....	35
From \$50.01 to \$100.....	55
From \$100.01 to \$165.....	60

C. In country "Bulgaria," under Parcel Post, amend the item *Prohibitions and import restrictions* to read as follows:

Prohibitions and import restrictions. The articles prohibited in the postal union mail and are prohibited as parcel post.

Gift shipments mailed by commercial firms.

Medicines not approved by the Bulgarian Ministry of Health.

Import licenses are required for all commercial parcels, and for gift parcels if the customs duty thereon exceeds 100 leva.

Used clothing must be accompanied by a certificate of disinfection. A notarized statement by a laundry or dry cleaner attesting that the clothing has been cleaned should meet the requirements of the Bulgarian Government.

D. Delete the country "Labuan" and the accompanying data. North Borneo includes Labuan and is now a part of "Malaysia Federation of".

E. Delete the country "Persian Gulf Ports" and the accompanying data and insert in proper alphabetical order the countries "Bahrein", "Muscat", "Qatar (Including Doha and Umm Said)" and "Trucial States (Including Abu Dhabi, Dubai and Sharjah)", with the following accompanying data thereunder.

Postal Union Mail

Surface rates, classifications, weight limits and dimensions. See § 168.1.

Air rates. (See § 168.1 for classifications, weight limits and dimensions.)

Letters, 25 cents per half ounce.
Single post cards, 11 cents each.
Aerogrammes, 11 cents each.
Other articles, 50 cents first 2 ounces; 30 cents each additional 2 ounces or fraction.

Small packets. Accepted.
Letter packages containing dutiable merchandise. Accepted. See § 112.1(e) of this chapter. Perishable biological material accepted. See § 111.3(b) (5) of this chapter.

Registration. Fee, 60 cents. Maximum indemnity, \$8.17.

Special delivery. No service.
Money orders. Yes. See § 61.2 of this chapter.

Prohibitions. Articles prohibited or restricted as parcel post are prohibited or restricted in the postal union mail.

Parcel Post

Surface parcel rates. Two pounds or less, 90 cents; each additional pound or fraction, 35 cents.

Air parcel rates. Four ounces or less, \$1.54; each additional pound or fraction, 65 cents

Weight limit: 22 pounds.
Sealing: Insured parcels must, and ordinary parcels may be sealed.
Group shipments: No.
Registration: No.
Insurance: Yes.
Postal forms required:
1 Form 2922.
2 Form 2966.
1 Form 2972.

Dimensions. Length, 3½ feet; length and girth combined, 6 feet.

Special handling. Available. See § 168.4.

Insurance. The following insurance fees and limits of indemnity apply:

Limit of indemnity:	Fee, cents
Not over \$10.....	20
From \$10.01 to \$25.....	25
From \$25.01 to \$50.....	35
From \$50.01 to \$100.....	55

Print on the wrapper, near the "Insured" endorsement and number, the amount for which the parcel is insured. This indication shall be shown in United States currency, in figures and in letters spelled out in full, in the following form:

INSURED VALUE

\$76.75

SEVENTY-SIX DOLLARS AND SEVENTY-FIVE CENTS

Parcels containing coins, bullion, precious stones, and any article of gold, silver, or platinum must be insured. Parcels containing jewelry must not have a value exceeding \$100.

The final decision on all questions of compensation rests with the country in whose service the loss, rifling, or damage took place.

For general information in insurance, see Part 133 of this chapter.

Prohibitions. Arms and parts thereof. Cultivated, imitation, artificial, or bleached pearls.

Coins and gold ingots exceeding \$5 (\$14) in value, except coins declared to be intended as ornaments. Silver ingots or partially worked silver exceeding \$20 (\$56) in value.

Carbon paper, oilskins, and similar goods are subject to the conditions applicable to such articles for Great Britain.

(R.S. 161, as amended; 5 U.S.C. 22, 39 U.S.C. 501, 505)

LOUIS J. DOYLE,
General Counsel.

[F.R. Doc. 64-4626; Filed, May 7, 1964; 8:48 a.m.]

Title 41—PUBLIC CONTRACTS**Chapter 50—Division of Public Contracts, Department of Labor****PART 50-204—SAFETY AND HEALTH STANDARDS FOR FEDERAL SUPPLY CONTRACTS****Radiation; AEC Contractors Operating AEC Plants and Facilities**

Amendments to 41 CFR Part 50-204 establishing radiation safety and health standards became effective on February 28, 1964 (29 F.R. 1437). Their application was, however, withheld as to contractors with the Atomic Energy Commission operating plants and facilities owned by the Commission pending further consideration of whether any special provision should be made in the regulations for such plants. The only parties that have expressed interest in

this matter have recently notified the Department that adoption of the proposed special provision for such contractors published in the FEDERAL REGISTER on November 8, 1963 (28 F.R. 11935) would be a satisfactory final disposition of the matter.

Accordingly, pursuant to authority in sections 1 and 4 of the Walsh-Healey Public Contracts Act (41 U.S.C. 35 and 38), and section 7(d) of the Administrative Procedure Act (5 U.S.C. 1006), I hereby amend 41 CFR 50-204.320, effective immediately, by changing the heading of the section, using the present heading and text as the heading and text of paragraph (a), and adding a new paragraph (b) to read as follows:

§ 50-204.320 AEC licensees; AEC contractors operating AEC plants and facilities.

(b) *AEC contractors operating AEC plants and facilities.* Any employer who

possesses or uses source material, by-product material, special nuclear material, or other radiation sources under a contract with the Atomic Energy Commission for the operation of AEC plants and facilities and in accordance with the standards, procedures, and other requirements for radiation protection established by the Commission for such contract pursuant to the Atomic Energy Act of 1954 as amended (42 U.S.C. 2011 et seq.), shall be deemed to be in compliance with the requirements of this part with respect to such possession and use.

(Secs. 1, 4, 49 Stat. 2036, 2038; 41 U.S.C. 35, 38; Sec. 7, 60 Stat. 241; 5 U.S.C. 1006)

Signed at Washington, D.C., this 4th day of May 1964.

W. WILLARD WIRTZ,
Secretary of Labor.

[F.R. Doc. 64-4623; Filed, May 7, 1964; 8:47 a.m.]

Proposed Rule Making

DEPARTMENT OF LABOR

Wage and Hour Division

[29 CFR Part 657]

[Administrative Order No. 581]

TOBACCO INDUSTRY IN PUERTO RICO

Review Committee; Appointment, Convention, and Notice of Hearing

Pursuant to section 5 of the Fair Labor Standards Act of 1938 (29 U.S.C. 205), Reorganization Plan No. 6 of 1950 (3 CFR 1949-53 Comp., p. 1004), and paragraph (C) of Proviso (1) of section 6(c) of the aforementioned Act, I hereby appoint Review Committee 8 for the tobacco industry in Puerto Rico (as defined in 29 CFR 657.1), to recommend the minimum wage rate or rates to be paid under paragraph (C) of Proviso (1) of subsection 6(c) of the aforementioned Act in lieu of those provided under paragraph (B) of Proviso (1) to employees in the industry.

Pursuant to sections 6 and 8 of the Fair Labor Standards Act of 1938 (29 U.S.C. 206, 208), and Reorganization Plan No. 6 of 1950, I hereby:

(1) Convene the review committee appointed above;

(2) Refer to it the question of the minimum rate or rates of wages to be fixed for the tobacco industry in Puerto Rico.

(3) Give notice of the hearing to be held by the review committee at the time and place indicated below. The Committee shall investigate conditions in the industry, and the committee, or any authorized subcommittee thereof, shall hear such witnesses and receive such evidence as may be necessary or appropriate

to enable the committee to perform its duties and functions under the aforementioned Act. The committee shall recommend to the Administrator the highest minimum wage rate or rates which it determines, having due regard to economic and competitive conditions, will not substantially curtail employment in the industry, and will not give any industry in Puerto Rico a competitive advantage over any industry in the United States outside of Puerto Rico, the Virgin Islands, and American Samoa.

Review Committee 8 shall meet in executive session to commence its investigation at 10:00 a.m. on May 25, 1964, in the office of the Wage and Hour and Public Contracts Divisions, United States Department of Labor, seventh floor, Condominio San Alberto Building, 1200 Ponce de Leon Avenue, Santurce, Puerto Rico, and shall commence its hearing at 1:30 p.m. on the same date at the same place.

If the review committee finds that a higher minimum wage may be determined for employees engaged in certain activities or in the manufacture of certain products in the industry than may be determined for other employees in it, the committee shall recommend such reasonable classifications within the industry as it determines to be necessary for the purpose of fixing for each classification the highest minimum wage rate that can be determined for it under the principles set forth herein which will not give a competitive advantage to any group in the industry. No classification shall be made, however, and no minimum wage rate shall be fixed solely on a regional basis or on the basis of age or sex. In determining whether there should be classifications within the industry, in making such classifications,

and in determining the minimum wage rates for such classifications, the review committee shall consider, among other relevant factors, the following: (1) Competitive conditions as affected by transportation, living, and production costs; (2) wages established for work of like or comparable character by collective labor agreements negotiated between employers and employees by representatives of their own choosing; and (3) wages paid for work of like or comparable character by employers who voluntarily maintain minimum wage standards in the industry.

The Administrator shall prepare an economic report for the committee containing such data as he is able to assemble pertinent to the matters referred to it. Copies of the report may be obtained at the National and Puerto Rican Offices of the United States Department of Labor as soon as it is completed and prior to the hearing. The committee will take official notice of the facts stated in the economic report to the extent they are not refuted by evidence received at the hearing.

The procedure for the review committee shall be governed by Parts 511 and 512 of Title 29, Code of Federal Regulations (28 F.R. 5644, June 8, 1963).

As a prerequisite to participation in the hearing of Review Committee 8, interested persons shall file prehearing statements containing the data specified in 29 CFR 511.8 not later than May 21, 1964.

Signed at Washington, D.C., this 5th day of May 1964.

W. WILLARD WIRTZ,
Secretary of Labor.

[F.R. Doc. 64-4624; Filed, May 7, 1964; 8:48 a.m.]

Notices

DEPARTMENT OF THE INTERIOR

Bureau of Indian Affairs YAKIMA PUBLIC DOMAIN ALLOTMENTS

Transfer of Land Records to Portland Area Office

MAY 4, 1964.

In accordance with 25 CFR Part 120 and pursuant to authority delegated by Amendment No. 49 to Secretarial Order 2508 (26 F.R. 11395), notice is hereby given that all source title documents and land records pertaining to the Yakima Public Domain Allotments in the State of Washington, have been transferred from the City of Washington, D.C., to the Portland Area Office, Bureau of Indian Affairs, 1002 Northeast Holliday Street, Portland, Oregon.

Effective May 1, 1964, the Portland Area Office will be the office for the maintenance of records for these trust and restricted lands.

JOHN O. CROW,
Acting Commissioner.

[F.R. Doc. 64-4606; Filed, May 7, 1964;
8:46 a.m.]

Bureau of Mines

CERTAIN ASSISTANT DIRECTORS

Redelegation of Authority

The following redelegation is a portion of the Bureau of Mines Manual and the numbering system is that of the Manual.

[Bureau of Mines Release No. 800]

PART 205—GENERAL DELEGATIONS

Sec. 205.5.8 *Leases*. By Secretary's Order No. 2509, Amendment 25, July 11, 1957, the Director may, within the continental limits of the United States and outside the District of Columbia, lease space in buildings that is to be used wholly or predominantly for the special purposes of the Bureau and will not be generally suitable for the use of other purposes, or that is required for use incidental to and in conjunction with space that will be used for such special purposes, or that is to be acquired under a lease involving no rental or nominal consideration of \$1.00 each year. The Director may, in the Territories and possessions of the United States, lease space in buildings either for the general purposes or for the special purposes of the Bureau. The authority is redelegated to the Assistant Director—Administration.

Sec. 205.10.1 *Quarters*. The authority with respect to quarters for employee housing under one's jurisdiction is redelegated to the Assistant Director—Administration and the Assistant Director—Helium to:

A. Require employees to occupy Government quarters, in accordance with 5 U.S.C. 75a-1 and 424 DM 3.2.

B. Fix rates for quarters, and for utilities, subsistence, furnishings, and services provided in connection with quarters, in accordance with 424 DM.

C. Make the determinations contemplated by paragraphs 2b and 2c of Bureau of the Budget Circular A-18, Revised, October 18, 1957, and by footnote number 4, page 6, of such circular. This authority must be exercised in accordance with 424 DM and current instructions on budget preparation. This authority may not be redelegated.

D. Make the determination as to when furnished rather than unfurnished quarters shall be provided in the United States, or when unfurnished rather than furnished quarters shall be provided outside the United States, in accordance with 424 DM. Such officials are also authorized to determine when furnishings may be provided in non-Government housekeeping quarters located in Alaska, Hawaii, and in specific areas outside of the United States, in accordance with Bureau of the Budget Circular A-15, Revised. This authority may not be redelegated.

Sec. 205.10.2 *Abandonment or destruction*. Authority is redelegated to the Assistant Director—Administration to abandon, destroy, or donate to public bodies, real property with no commercial value, or real property the estimated cost of continued care and handling of which would exceed the estimated proceeds from its sales, as authorized by and in full compliance with Chapter VII, Title 2, Regulations of the General Services Administration.

Sec. 205.11.1 *Formally advertised contracts*. The authority to enter into formally advertised contracts for supplies, equipment, and nonpersonal services (including construction) is redelegated to the Assistant Director—Administration and Headquarters Chief, Division of Procurement and Property Management; to all other Assistant Directors, and Chiefs, Eastern and Western Administrative Offices, in amounts not to exceed \$100,000 for any one contract. The authority delegated herein shall be exercised in accordance with the applicable limitations in the Federal Property and Administrative Services Act of 1949, as amended, and in accordance with applicable policies, procedures, and controls prescribed by the General Services Administration, the Department of the Interior, and the Bureau of Mines.

Sec. 205.11.4 *Negotiated contracts*. The authority to enter into negotiated contracts under sections 302(c) (1) through (10) and (13) through (15) of the Federal Property and Administrative Services Act of 1949, as amended, provided that any one contract negotiated under section 302(c) (1) shall not

exceed \$25,000, is redelegated to the Assistant Director—Administration and Headquarters Chief, Division of Procurement and Property Management.

The authority to enter into negotiated contracts under sections 302(c) (1) through (5), (10), (13), and (14) of the Federal Property and Administrative Services Act of 1949, as amended, in amounts not to exceed \$100,000 for any one contract except that any one contract negotiated under section 302(c) (1) shall not exceed \$25,000, is redelegated within the provisions of 205 BM 11.4 to the Assistant Director—Health and Safety, Assistant Director—Helium, Assistant Director—Mineral Resource Development, Assistant Director—Minerals Research, Chief, Eastern Administrative Office and Chief, Western Administrative Office. The authority delegated herein shall be exercised in accordance with the Federal Property and Administrative Services Act of 1949, as amended, and in accordance with applicable policies, procedures, and controls prescribed by the General Services Administration, the Department of the Interior, and the Bureau of Mines.

Sec. 205.25.1 *Land Acquisition; reimbursement for moving*. The Director is authorized to exercise the authority of the Secretary of the Interior under section 1 of the Act of May 29, 1958 (72 Stat. 152), relating to reimbursement of owners and tenants of lands acquired for Department programs for expenses and other losses and damages incurred by them in the process, and as a direct result of such moving of themselves, their families, and their possessions, as is occasioned by such acquisition (Secretary's Order No. 2840, dated April 28, 1959, 34 F.R. 3615). This authority is redelegated to the Assistant Director—Administration.

MARLING J. ANKENY,
Director, Bureau of Mines.

[F.R. Doc. 64-4607; Filed, May 7, 1964;
8:46 a.m.]

DEPARTMENT OF COMMERCE

Bureau of International Commerce

[Case 326]

IRVING BETHEIL ET AL.

Order Denying Export Privileges

In the matter of Irving Bethel, International American Forwarding Corporation, 38 Pearl Street, New York, New York; Sylvan L. Hart, a/k/a Sylvan L. Hayuth, d/b/a Sela Electronics Company, 545 West End Avenue, New York, New York; Fred R. Gluckman, 140 Riverside Drive, New York, New York; Case No. 326; respondents.

The above respondents were, on February 6, 1964, charged by the Director, Investigations Division, Office of Export

Control, Bureau of International Commerce, with violations of the Export Control Act of 1949, as amended, and regulations thereunder. The respondents were served with the charging letter. The respondent Hart has failed to file an answer or to respond to the charges and he is held to be in default. The respondents Bethell, International American Forwarding Corporation, and Gluckman have filed answers.

Prior to the issuance of the charging letter, an order temporarily denying export privileges was issued against the respondents Hart and Gluckman, on December 31, 1963 (29 F.R. 56, January 3, 1964). On February 26, 1964, said temporary order was extended until the completion of administrative compliance proceedings (29 F.R. 2914, March 3, 1964).

The respondent Bethell is president of International American Forwarding Corporation (International). It is charged that Bethell acting individually and for International, on February 13, 1963, as freight forwarder for a foreign firm, and on June 14, 1963, as forwarding agent for Sela Electronics Company, exported from the United States to Austria oscilloscopes and other electronic equipment. As to the February 13, 1963 exportation it is alleged that these respondents falsely described the commodities and gave an incorrect classification number, thereby representing that the commodities were exportable under General License. As to the June 14, 1963 exportation it is alleged that they exported the commodities without applying for or obtaining the required validated export license and that they failed to produce the records of this export transaction when requested to do so by proper authorities. It is further charged that these respondents on January 8, 1964, acting as freight forwarder for a Brazilian firm, exported sundry commodities falsely describing them as agricultural equipment and grossly understating their value.

There are three charges against Gluckman in which it is alleged that he acted individually and for respondent Sela Electronics Company. It is alleged that on June 28, 1963, July 7, 1963 and July 12, 1963, he exported from the United States to Austria by parcel post various quantities of electronic tubes and diodes without applying for and obtaining validated licenses authorizing the exportations and without presenting to the Postmaster at New York City validated licenses and Shipper's Export Declarations covering the exportations of said commodities.

There are three charges against Hart wherein it is alleged that he acted individually and for Sela Electronics Company. It is alleged that on February 1, 1963, April 8, 1963 and April 23, 1963, he exported via parcel post from the United States to Austria electronic tubes, diodes and other strategic items without applying for and obtaining validated licenses authorizing the exportations and without presenting to the Postmaster at New York City validated licenses and Shipper's Export Declarations covering the exportations of said commodities.

It is charged that the respondents violated certain specific sections of the U.S. Export Regulations.

In accordance with the provisions of § 382.10 of the Export Regulations, with agreement of the Director, Investigations Division, the respondents Bethell and International, and also Gluckman, have submitted to the Compliance Commissioner proposals for a consent order substantially in the form hereinafter set forth. In the consent proposals, said respondents have admitted, for the purpose of these compliance proceedings, the allegations in the charging letter.

The Compliance Commissioner has reviewed the facts in the case and the consent proposals. He has approved the proposals and has submitted his recommendation to the undersigned Director, Office of Export Control, that the consent proposals be accepted. He has also recommended that sanctions as herein-after set forth be imposed against Hart, d/b/a Sela Electronics Company. After reviewing and considering the record in the case and the Compliance Commissioner's recommendations, I hereby make the following findings of fact:

1. The respondent International American Forwarding Corporation (International) is engaged in the freight forwarding business and has a place of business in New York City, the respondent Irving Bethell is president of said Corporation and is the individual responsible for its operations and management. The respondent Sylvan L. Hart, also known as Sylvan L. Hayuth, is an electronic engineer and owns and operates the firm known as Sela Electronics Company (Sela) in New York City. The respondent Fred R. Gluckman is a resident of New York City.

2. On February 13, 1963, Bethell acting individually and for respondent International, as freight forwarder for a foreign company, exported from the United States to Austria, three oscilloscopes which required validated export licenses from the Office of Export Control, Department of Commerce, for such exportation. Said respondents falsely described the oscilloscopes on the Shipper's Export Declaration and falsely described them under an incorrect classification number, thereby representing that said commodities were exportable from the United States to Austria under General License GRO.

3. On June 14, 1963, Bethell acting individually and for respondent International, as forwarding agent for the respondent Hart, d/b/a Sela, exported from the United States to Austria, two oscilloscopes with accessories and a signal generator. Said commodities required validated export licenses from the Office of Export Control, Department of Commerce, for said exportation. Said respondents did not apply for or obtain the necessary validated licenses before making the exportation. The respondents failed to produce the records concerning this export transaction when requested to do so by an authorized agent of the Bureau of International Commerce, Department of Commerce.

4. On January 8, 1964, Bethell acting individually and for respondent Inter-

national, as freight forwarder for a Brazilian company, exported from the United States to Brazil a shipment of sundry commodities, all of non-strategic nature, having an aggregate value of \$95,000, falsely describing them on Shipper's Export Declaration as agricultural equipment and falsely certifying the value as \$1,500.

5. On June 28, 1963, July 7, 1963, and July 12, 1963 the respondent Gluckman, acting individually and for the respondent Hart, d/b/a Sela, exported from the United States to Austria by parcel post, a total of 180 electronic tubes and diodes. Said commodities required validated export licenses from the Office of Export Control for exportation and said respondent did not apply for or obtain the required export licenses. Said respondent made the exportations without presenting to the Postmaster at New York City, the place of exportations, validated export licenses or duly executed Shipper's Export Declarations covering said commodities, as required by the Export Regulations.

6. On February 1, 1963, April 8, 1963 and April 23, 1963 the respondent Hart acting individually and for his firm Sela, exported from the United States to Austria, by parcel post, six electronic tubes and diodes, and a quantity of strategic material in semifabricated form. Said commodities required validated export licenses from the Office of Export Control for exportation and said respondent did not apply for or obtain the required export licenses. Said respondent made the exportations without presenting to the Postmaster at New York City, the place of exportations, validated export licenses or duly executed Shipper's Export Declarations covering said commodities, as required by the Export Regulations.

From the foregoing I have concluded that the respondents Bethell and International caused false representations to be made to, and material facts to be concealed from, the U.S. Department of Commerce and the U.S. Collector of Customs in connection with the preparation and use of export control documents in effecting the exportation of commodities from the United States; exported from the United States to Austria certain commodities subject to the U.S. Export Regulations without having obtained from the Department of Commerce the validated export license required to authorize such exportations; failed to produce and make available records, which said respondents were required to keep when requested to do so by an authorized agent of the Bureau of International Commerce, all in violation of §§ 370.2, 372.3, 381.2, 381.3(b), 381.4, 381.5, 381.6 and 381.11 of the U.S. Export Regulations. I have further concluded that the respondents Gluckman and Hart exported commodities from the United States to Austria without having presented to the Postmaster at New York City, the place of mailing, validated licenses which were required for said exportations together with related duly executed Shipper's Export Declarations covering said commodities, all in violation of §§ 370.2(b), 371.10, 372.3, 379.1

(b), 381.2 and 381.4 of the U.S. Export Regulations.

Now after considering the record in the case, the proposals for consent orders, and the recommendations of the Compliance Commissioner, and being of the view that this order is calculated to achieve effective enforcement of the law and the purposes thereof: *It is hereby ordered,*

I. All outstanding validated export licenses in which respondents Irving Bethell or International American Forwarding Corporation appear or participate in any manner or capacity are hereby revoked and shall be returned forthwith to the Bureau of International Commerce for cancellation. Such validated export licenses as may be outstanding in which respondents Sylvan L. Hart, also known as Sylvan L. Hayuth, doing business as Sela Electronics Company, or Fred R. Gluckman appear or participate in any manner or capacity and which have heretofore been revoked shall be returned to said Bureau for cancellation.

II. Except as qualified in Part IV hereof, the respondents Irving Bethell and International American Forwarding Corporation, for a period of 54 months from the effective date of this order, the respondent Fred R. Gluckman for a period of 30 months from the effective date of this order, and the respondent Sylvan L. Hart, also known as Sylvan L. Hayuth, doing business as Sela Electronics Company, for the duration of export controls, are hereby denied all privileges of participating, directly or indirectly, in any manner or capacity, in any transaction involving commodities or technical data exported from the United States in whole or in part, or to be exported, or which are otherwise subject to the Export Regulations. Without limitation of the generality of the foregoing, participation prohibited in any such transaction either in the United States or abroad shall include participation: (a) As a party or as a representative of a party to any validated export license application; (b) in the preparation or filing of any export license application or reexportation authorization, or document to be submitted therewith; (c) in the obtaining or using of any validated or general export license or other export control documents; (d) in the carrying on of negotiations with respect to, or in the receiving, ordering, buying, selling, delivering, storing, using, or disposing of any commodities or technical data; (e) in the financing, forwarding, transporting, or other servicing of such commodities or technical data.

III. Such denial of export privileges shall extend not only to the respondents, but also to their successors or assigns, officers, partners, representatives, agents, and employees, and also to any person, firm, corporation, or other business organization with which they now or hereafter may be related by affiliation, ownership, control position of responsibility, or other connection in the conduct of trade or services connected therewith.

IV. (a) Six months after the effective date of this order, without further order of the Bureau of International Com-

merce, the respondents Irving Bethell, International American Forwarding Corporation, and Fred R. Gluckman shall have their export privileges restored to them conditionally and thereafter for the remainder of the respective denial periods the said respondents shall be on probation. However, no validated licenses which have been revoked under this order or under the temporary denial order of December 31, 1963 shall thereby be restored. The conditions of such restoration are that the respondents shall fully comply with all requirements of the Export Control Act of 1949, as amended, and all regulations, licenses and orders issued thereunder.

(b) Two years after the effective date hereof the respondent Sylvan L. Hart, also known as Sylvan L. Hayuth, doing business as Sela Electronics Company, may apply to have the effective denial of his export privileges held in abeyance while he remains on probation. Such application shall be supported by evidence showing compliance with the terms of this order and such disclosure of details of his activities during said two years as may be necessary to determine his compliance with this order. The application will be considered on its merits and in the light of conditions and policies existing at that time. His export privileges may be restored under such terms and conditions as appear to be appropriate.

V. Upon a finding by the Director, Office of Export Control, or such other official as may be exercising the duties now exercised by him, that the respondents Bethell, International American Forwarding Corporation or Gluckman have knowingly failed to comply with the requirements and conditions of this order or with the conditions of probation, said official at any time, with or without prior notice to said respondent, by supplemental order, may revoke the probation of said respondent, revoke all outstanding validated export licenses to which any of said respondents may be a party, and deny all export privileges, for a period up to 48 months as to Bethell and International American Forwarding Corporation, and for a period up to 24 months as to Gluckman. Such order shall not preclude the Bureau of International Commerce from taking further action for any violation as shall be warranted. Any person affected by a supplemental order revoking without notice his probation, may file objections and request that such order be set aside, and may request an oral hearing, as provided in § 382.16 of the Export Regulations, but pending such further proceedings, the order of revocation shall remain in effect.

VI. During the time when any respondent or other person within the scope of this order is prohibited from engaging in any activity within the scope of Part II hereof, no person, firm, corporation, partnership, or other business organization, whether in the United States or elsewhere, without prior disclosure to and specific authorization from the Bureau of International Commerce, shall do any of the following acts, directly or indirectly, in any manner or

capacity, on behalf of or in any association with any respondent or other person denied export privileges within the scope of this order, or whereby any such respondent or such other person may obtain any benefit therefrom or have any interest or participation therein, directly or indirectly: (a) Apply for, obtain, transfer, or use any license, shipper's export declaration, bill of lading, or other export control document relating to any exportation, reexportation, transshipment, or diversion of any commodity or technical data exported or to be exported from the United States, by, to, or for any such respondent or other person denied export privileges within the scope of this order; or (b) order, buy, receive, use, sell, deliver, store, dispose of, forward, transport, finance, or otherwise service or participate in any exportation, reexportation, transshipment, or diversion of any commodity or technical data exported or to be exported from the United States.

This order shall become effective on May 1, 1964.

FORREST D. HOCKERSMITH,
Director,
Office of Export Control.

[F.R. Doc. 64-4631; Filed, May 7, 1964;
8:49 a.m.]

Office of the Secretary
GEORGE L. WILSON

Statement of Changes in Financial Interests

In accordance with the requirements of section 710(b)(6) of the Defense Production Act of 1950, as amended, and Executive Order 10647 of November 28, 1955, the following changes have taken place in my financial interests as reported in the FEDERAL REGISTER during the past six months:

- A. Deletions: No change.
- B. Additions: No change.

This statement is made as of April 20, 1964.

GEORGE L. WILSON.

APRIL 20, 1964.

[F.R. Doc. 64-4632; Filed, May 7, 1964;
8:49 a.m.]

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

Food and Drug Administration
BUCKMAN LABORATORIES, INC.

Notice of Filing of Petition Regarding Food Additives

Pursuant to the provisions of the Federal Food, Drug, and Cosmetic Act (sec. 409(b)(5), 72 Stat. 1786; 21 U.S.C. 348 (b)(5)), notice is given that a petition (FAP 1368) has been filed by Buckman Laboratories, Inc., 1256 North McLean, Memphis, Tennessee, 38108, proposing that § 121.2505 *Stimicides* be amended as follows:

1. By inserting alphabetically in the list of slime-control substances in paragraph (c) the new item "2-Bromo-4'-hydroxyacetophenone."

2. By inserting alphabetically in the list of adjuvant substances in paragraph (d) the new items "Butylene oxide" and "Monomethyl ethers of mono-, di-, and tripropylene glycol."

Dated: May 1, 1964.

MALCOLM R. STEPHENS,
Assistant Commissioner
for Regulations.

[F.R. Doc. 64-4629; Filed, May 7, 1964;
8:49 a.m.]

CIVIL AERONAUTICS BOARD

[Docket 13777; Order 20758, Corrected]¹

INTERNATIONAL AIR TRANSPORT ASSOCIATION

Agreement Relating to Specific Commodity Rates

Adopted by the Civil Aeronautics Board at its office in Washington, D.C., on the 28th day of April 1964.

There has been filed with the Board, pursuant to section 412(a) of the Federal Aviation Act of 1958 (the Act) and Part 261 of the Board's Economic Regulations, an agreement between various air carriers, foreign air carriers, and other carriers, embodied in the resolutions of Traffic Conference 1 of the International Air Transport Association (IATA), and adopted pursuant to the provisions of Resolution 590 (Commodity Rates Board).

This agreement, adopted pursuant to unprotested notices to the carriers and promulgated in IATA memoranda, extends the effectiveness of certain existing specific commodity rates as set forth in the attachment hereto.²

The Board, acting pursuant to sections 102, 204(a), and 412 of the Act, does not find the subject agreement to be adverse to the public interest or in violation of the Act, provided that approval thereof is conditioned as hereinafter ordered.

Accordingly, it is ordered: That Agreement C.A.B. 17666, R-2, be and hereby is approved, provided that such approval shall not constitute approval of the specific commodity descriptions contained therein for purposes of tariff publication.

Any air carrier party to the agreement, or any interested person, may, within 15 days from the date of service of this order, submit statements in writing containing reasons deemed appropriate, together with supporting data, in support of or in opposition to the Board's action herein. An original and nineteen copies of the statements should be filed with the Board's Docket Section. The Board may, upon consideration of any such statements filed, modify or rescind its action herein by subsequent order.

¹ To correct conference and docket numbers.

² Filed as part of the original document.

This order will be published in the FEDERAL REGISTER.

By the Civil Aeronautics Board.

[SEAL] HAROLD R. SANDERSON,
Secretary.

[F.R. Doc. 64-4633; Filed, May 7, 1964;
8:49 a.m.]

[Docket 14792]

NORTH CENTRAL RENEWAL OF CERTAIN SEGMENT

Notice of Prehearing Conference

Renewal North Central's Segment 12. Notice is hereby given that a prehearing conference in the above-entitled matter is assigned to be held on June 2, 1964, at 10 a.m., e.d.s.t., in Room 1027, Universal Building, Connecticut and Florida Avenues NW., Washington, D.C., before Examiner Leslie G. Donahue.

Dated at Washington, D.C., May 6, 1964.

[SEAL] FRANCIS W. BROWN,
Chief Examiner.

[F.R. Doc. 64-4634; Filed, May 7, 1964;
8:50 a.m.]

FEDERAL COMMUNICATIONS COMMISSION

[Docket Nos. 15323-15325; FCC 64R-248]

INTEGRATED COMMUNICATIONS SYSTEMS, INC., OF MASSACHUSETTS ET AL.

Memorandum Opinion and Order Amending Issues

In re applications of Integrated Communication Systems, Inc. of Massachusetts, Boston, Massachusetts, Docket No. 15323, File No. BPCT-3167; United Artists Broadcasting, Inc., Boston, Massachusetts, Docket No. 15324, File No. BPCT-3169; WGBH Educational Foundation, Boston, Massachusetts, Docket No. 15325, File No. BPCT-3277; for construction permits for new television broadcast stations.

1. United Artists Broadcasting, Inc. (United Artists) petitions the Review Board to enlarge issues in this proceeding.¹ Petitioner seeks the addition of the following issues with respect to the application of Integrated Communication Systems, Inc. of Massachusetts (Integrated):

(a) To determine whether the applicant, in view of its proposal as to staff, is qualified to operate its station in the manner proposed in its application.

(b) To determine whether the program proposals of the applicant are fea-

¹ The pleadings before the Review Board include: (1) Motion to enlarge issues, filed Mar. 2, 1964, by United Artists Broadcasting, Inc.; (2) Opposition, filed Apr. 8, 1964, by Integrated Communication Systems, Inc. of Massachusetts; (3) Response, filed Apr. 8, 1964, by the Broadcast Bureau; and (4) Reply to opposition, filed Apr. 20, 1964, by petitioner.

sible for a UHF television station without network affiliation in the Boston market; whether there is a reasonable prospect that the program proposals can be effectuated; and, in light of evidence adduced with respect to the foregoing, whether the applicant is qualified to operate its station in the manner proposed in its application.

2. This proceeding involves mutually exclusive applications for a new UHF television broadcast station in Boston, Massachusetts. United Artists challenges the adequacy of the staff proposed by Integrated. To support its contention, petitioner points out that Integrated contemplates a weekly schedule totalling 45½ hours, of which 45 percent, or more than 20 hours, is to be local live programming. United Artists asserts that Integrated proposes local live programs on each day of the week with six such programs on Mondays through Fridays and also on Sundays, and five live programs on Saturdays. In order to maintain this schedule, petitioner indicates that a staff of thirteen employees is designated by Integrated, including five management personnel. According to United Artists, the remaining eight staff members are to work in the engineering, business, commercial and program departments; however, it is noted by petitioner, no allocation of these staff members is provided by Integrated in its application. In light of personnel requirements and viewed most favorably to Integrated, United Artists contends that no more than four staff members can be considered as available for the program department which is primarily responsible for the heavy work load imposed by over 20 hours of local live programming per week. Petitioner notes that none of Integrated's principals have television broadcast experience and that Integrated's proposed percentage of live broadcasts exceeds that shown in the renewal applications of all but one television station out of 491 stations surveyed in Veterans Broadcasting Company, Inc., Docket No. 14367 et al. (Six Nations Rebuttal Exhibit No. 1). United Artists also challenges the feasibility of the program proposals advanced by Integrated in light of the following considerations: (1) Integrated has applied for a UHF channel in a market with three VHF network affiliates; (2) Integrated has proposed programming which would be extraordinarily ambitious, even for a profitable VHF station; (3) Integrated's operating budget is based on an inadequate staff proposal; and (4) operating revenues are proposed to cover substantial long-term debt retirement. Petitioner urges that adequate exploration of the feasibility of Integrated's proposal cannot be made under the standard comparative issues or the standard financial qualifications and Evansville issues; therefore, the requested issues are necessary to develop an adequate record and to enable the Commission to evaluate the problems inherent in the introduction of a UHF station in an all-VHF market.

3. Integrated, in opposing the motion to enlarge issues, attempts to distinguish