

### § 1.263(a)-3

(d) The amount expended for architect's services.

(e) Commissions paid in purchasing securities. Commissions paid in selling securities are an offset against the selling price, except that in the case of dealers in securities such commissions may be treated as an ordinary and necessary business expense.

(f) Amounts assessed and paid under an agreement between bondholders or shareholders of a corporation to be used in a reorganization of the corporation or voluntary contributions by shareholders to the capital of the corporation for any corporate purpose. Such amounts are capital investments and are not deductible. See section 118 and § 1.118-1.

(g) A holding company which guarantees dividends at a specified rate on the stock of a subsidiary corporation for the purpose of securing new capital for the subsidiary and increasing the value of its stockholdings in the subsidiary shall not deduct amounts paid in carrying out this guaranty in computing its taxable income, but such payments are capital expenditures to be added to the cost of its stock in the subsidiary.

(h) The cost of good will in connection with the acquisition of the assets of a going concern is a capital expenditure.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 8131, 52 FR 10084, Mar. 30, 1987]

### § 1.263(a)-3 Election to deduct or capitalize certain expenditures.

(a) Under certain provisions of the Code, taxpayers may elect to treat capital expenditures as deductible expenses or as deferred expenses, or to treat deductible expenses as capital expenditures.

(b) The sections referred to in paragraph (a) of this section include:

(1) Section 173 (circulation expenditures).

(2) Section 174 (research and experimental expenditures).

(3) Section 175 (soil and water conservation expenditures).

(4) Section 177 (trademark and trade name expenditures).

(5) Section 179 (election to expense certain depreciable business assets).

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(6) Section 180 (expenditures by farmers for fertilizer, lime, etc.).

(7) Section 182 (expenditures by farmers for clearing land).

(8) Section 248 (organizational expenditures of a corporation).

(9) Section 266 (carrying charges).

(10) Section 615 (exploration expenditures).

(11) Section 616 (development expenditures).

[T.D. 6500, 25 FR 11402, Nov. 26, 1960, as amended by T.D. 6794, 30 FR 792, Jan. 26, 1965; T.D. 8121, 52 FR 414, Jan. 6, 1987]

### § 1.263(b)-1 Expenditures for advertising or promotion of good will.

See § 1.162-14 for the rules applicable to a corporation which has elected to capitalize expenditures for advertising or the promotion of good will under the provisions of section 733 or section 451 of the Internal Revenue Code of 1939, in computing its excess profits tax credit under Subchapter E, Chapter 2, or Subchapter D, Chapter 1, of the Internal Revenue Code of 1939.

### § 1.263(c)-1 Intangible drilling and development costs in the case of oil and gas wells.

For rules relating to the option to deduct as expenses intangible drilling and development costs in the case of oil and gas wells, see § 1.612-4.

### § 1.263(e)-1 Expenditures in connection with certain railroad rolling stock.

(a) *Allowance of deduction*—(1) *Election*. Under section 263(e), for any taxable year beginning after December 31, 1969, a taxpayer may elect to treat certain expenditures paid or incurred during such taxable year as deductible repairs under section 162 or 212. This election applies only to expenditures described in paragraph (c) of this section in connection with the rehabilitation of a unit of railroad rolling stock (as defined in paragraph (b)(2) of this section) used by a domestic common carrier by railroad (as defined in paragraph (b) (3) and (4) of this section). However, an election under section 263(e) may not be made with respect to expenditures in connection with any unit of railroad rolling stock for which an election under section 263(f) and the

regulations thereunder is in effect. An election made under section 263(e) is an annual election which may be made with respect to one or more of the units of railroad rolling stock owned by the taxpayer.

(2) *Special 20 percent rule.* Section 263(e) shall not apply if, under paragraph (d) of this section, expenditures paid or incurred during any period of 12 calendar months in connection with the rehabilitation of a unit exceed 20 percent of the basis (as defined in paragraph (b)(1) of this section) of such unit in the hands of the taxpayer. However, section 263(e) does not constitute a limit on the deduction of expenditures for repairs which are deductible without regard to such section. Accordingly, amounts otherwise deductible as repairs will continue to be deductible even though such amounts exceed 20 percent of the basis of the unit of railroad rolling stock in the hands of the taxpayer.

(3) *Time and manner of making election.* (i) An election by a taxpayer under section 263(e) shall be made by a statement to that effect attached to its income tax return or amended income tax return for the taxable year for which the election is made if such return or amended return is filed no later than the time prescribed by law (including extensions thereof) for filing the return for the taxable year of election. An election under section 263(e) may be made with respect to one or more of the units of railroad rolling stock owned by the taxpayer. If an election is not made within the time and in the manner prescribed in this subparagraph, no election may be made (by the filing of an amended return or in any other manner) with respect to the taxable year.

(ii) If the taxpayer has filed a return on or before March 14, 1973, and has claimed a deduction under section 162 or 212 by reason of section 263(e), and if the taxpayer does not desire to make an election under section 263(e) for the taxable year with respect to which such return was filed, the taxpayer shall file an amended return for such taxable year on or before May 14, 1973, and shall pay any additional tax due for such year. The taxpayer shall also file an amended return for each taxable

year which is affected by the filing of an amended return under the preceding sentence and shall pay any additional tax due for such year. Nothing in this subdivision shall be construed as extending the time specified in section 6511 within which a claim for credit or refund may be filed.

(iii) If an election under section 263(e) was not made at the time the return for a taxable year was filed, and it is subsequently determined that an expenditure was erroneously treated as an expenditure which was not in connection with rehabilitation (as determined under paragraph (c) of this section), an election under section 263(e) may be made with respect to the unit of railroad rolling stock for which such expenditure was made for such taxable year, notwithstanding any provision in this subparagraph (3) to the contrary. Nothing in this subdivision shall be construed as extending the time specified in section 6511 within which a claim for credit or refund may be filed.

(iv) The statement required by subdivision (i) of this subparagraph shall include the following information:

(a) The total number of units of railroad rolling stock with respect to which an election is being made under section 263(e).

(b) The aggregate basis (as defined in paragraph (b) (1) of this section) of the units described in (a) of this subdivision (iv), and

(c) The total deduction being claimed under section 263(e) for the taxable year.

(b) *Definitions—(1) Basis.* (i) In general, for purposes of section 263(e) the basis of a unit of railroad rolling stock shall be the adjusted basis of such unit determined without regard to the adjustments provided in paragraphs (1), (2), and (3) of section 1016(a) and section 1017. Thus, the basis of property would generally be its cost without regard to adjustments to basis such as for depreciation or for capital improvements. If the basis of a unit in the hands of a transferee is determined in whole or in part by reference to its basis in the hands of the transferor, for example, by reason of the application of section 362 (relating to basis to corporations), 374 (relating to gain or loss

not recognized in certain railroad reorganizations), or 723 (relating to the basis of property contributed to a partnership), then the basis of such unit in the hands of the transferor for purposes of section 263(e) shall be its basis for purposes of section 263(e) in the hands of the transferee. Similarly, when the basis of a unit of railroad rolling stock in the hands of the taxpayer is determined in whole or in part by reference to the basis of another unit, for example, by reason of the application of the first sentence of section 1033(c) (relating to involuntary conversions), then the basis of the latter unit for purposes of section 263(e) shall be the basis for purposes of section 263(e) of the former unit. The question whether a capital expenditure in connection with a unit of railroad rolling stock results in the retirement of such unit and the creation of another unit of railroad rolling stock shall be determined without regard to rules under the uniform system of accounts prescribed by the Interstate Commerce Commission.

(ii) For example, if a unit of railroad rolling stock has a cost to M of \$10,000 and because of depreciation adjustments of \$4,000 and capital expenditures of \$3,000, such unit has an adjusted basis in the hands of M of \$9,000, the basis for purposes of section 263(e) of such unit in the hands of M is \$10,000. Further, if M transfers such unit to N in a transaction in which no gain or loss is recognized such as, for example, a transaction to which section 351(a) (relating to a transfer to a corporation controlled by the transferor) applies, the basis of such unit for purposes of section 263(e) is \$10,000 in the hands of N.

(2) *Railroad rolling stock.* For purposes of this section, the term *unit* or *unit of railroad rolling stock* means a unit of transportation equipment the expenditures for which are of a type chargeable (or in the case of property leased to a domestic common carrier by railroad, would be chargeable) to the equipment investment accounts in the uniform system of accounts for railroad companies prescribed by the Interstate Commerce Commission (49 CFR Part 1201), but only if (i) such unit exclusively moves on, moves under, or is guided by rail, and (ii) such unit is

not a locomotive. Thus, for example, a unit of railroad rolling stock includes a box car, a gondola car, a passenger car, a car designed to carry truck trailers and containerized freight, a wreck crane, and a bunk car. However, such term does not include equipment which does not exclusively move on, move under, or is not exclusively guided by rail such as, for example, a barge, a tugboat, a container which is used on cars designed to carry containerized freight, a truck trailer, or an automobile. A locomotive is self-propelled equipment, the sole function of which is to push or pull railroad rolling stock. Thus, a self-propelled passenger or freight car is not a locomotive.

(3) *Domestic common carrier by railroad.* The term *domestic common carrier by railroad* means a railroad subject to regulation under Part I of the Interstate Commerce Act (49 U.S.C. 1 *et seq.*) or a railroad which would be subject to regulation under Part I of the Interstate Commerce Act if it were engaged in interstate commerce.

(4) *Use.* For purposes of this section, a unit of railroad rolling stock is not used by a domestic common carrier by railroad if it is owned by a person other than a domestic common carrier by railroad and (i) is exclusively used for transportation by the owner or (ii) is exclusively used for transportation by another person which is not a domestic common carrier by railroad. Thus, for example, a unit of railroad rolling stock which is owned by a person which is not a domestic common carrier by railroad and is leased to a manufacturing company by the owner is not a unit of railroad rolling stock used by a domestic common carrier by railroad.

(c) *Expenditures considered in connection with rehabilitation.* For purposes of section 263(e) and this section all expenditures which would be properly chargeable to capital account but for the application of section 263 (e) or (f) shall be considered to be expenditures in connection with the rehabilitation of a unit of railroad rolling stock. Expenditures which are paid or incurred in connection with incidental repairs or maintenance of a unit of railroad rolling stock and which are deductible without regard to section 263 (e) or (f)

shall not be included in any determination or computation under section 263(e) and shall not be treated as paid or incurred in connection with the rehabilitation of a unit of railroad rolling stock for purposes of section 263(e). The determination of whether an item would be, but for section 263 (e) or (f), properly chargeable to capital account shall be made in a manner consistent with the principles for classification of expenditures as between capital and expenses under the Internal Revenue Code. See, for example, §§1.162-4, 1.263(a)-1, 1.263(a)-2, and paragraph (a)(4) (ii) and (iii) of §1.446-1. An expenditure shall be classified as capital or as expense without regard to its classification under the uniform system of accounts prescribed by the Interstate Commerce Commission.

(d) *20-percent limitation*—(1) *In general.* No expenditures in connection with the rehabilitation of a unit of railroad rolling stock shall be treated as a deductible repair by reason of an election under section 263(e) if, during any period of 12 calendar months in which the month the expenditure is included falls, all such expenditures exceed an amount equal to 20 percent of the basis (as defined in paragraph (b)(1) of this section) of such unit in the hands of the taxpayer. All such expenditures shall be included in the computation of the 20-percent limitation even if such expenditures were deducted under section 263(f) in either the preceding or succeeding taxable year. Solely for purposes of the 20-percent limitation in this paragraph, such expenditures shall be deemed to be included in the month in which a rehabilitation of the unit of railroad rolling stock is completed. For the requirement that expenditures treated as repairs solely by reason of an election under section 263(e) be deducted in the taxable year paid or incurred, see paragraph (a) of this section.

(2) *12-month period.* For purposes of this section, any period of 12 calendar months shall consist of any 12 consecutive calendar months except that calendar months prior to the calendar month of January 1970 shall not be included in determining such period.

(3) *Period for certain corporate acquisitions.* If a unit of railroad rolling stock

to which section 263(e) applies is sold, exchanged, or otherwise disposed of in a transaction in which its basis in the hands of the transferee is determined in whole or in part by reference to its basis in the hands of the transferor (see paragraph (b)(1) of this section), calendar months during which such unit is in the hands of the transferor and in the hands of such transferee shall both be included in the calendar months used by the transferor and the transferee to determine any period of 12 calendar months for purposes of section 263(e).

(4) *Deduction allowed in year paid or incurred.* If, based on the information available when the income tax return for a taxable year is filed, an expenditure paid or incurred in such taxable year would be deductible by reason of the application of section 263(e) but for the fact that it cannot be established whether the 20-percent limitation in subparagraph (1) of this paragraph will be exceeded, the expenditure shall be deducted for such taxable year. If by reason of the application of such 20-percent limitation it is subsequently determined that such expenditure is not deductible as a repair, an amended return shall be filed for the year in which such deduction was treated as a deductible repair and additional tax, if any, for such year shall be paid. Appropriate adjustment with respect to the taxpayer's tax liability for any other affected year shall be made. Nothing in this subparagraph shall be construed as extending the time specified in section 6511 within which a claim for credit or refund may be filed.

(e) *Recordkeeping requirements*—(1) *In general.* Such records as will enable the accurate determination of the expenditures which may be subject to the treatment provided in section 263(e) shall be maintained. No deduction shall be allowed under section 162 or 212 by reason of section 263(e) with respect to a unit unless the taxpayer substantiates by adequate records that expenditures in connection with such unit of railroad rolling stock meet the requirements and limitations of this section.

(2) *Separate records.* A separate section 263(e) record shall be maintained for each unit with respect to which an

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election under section 263(e) is made. Such record shall:

- (i) Identify the unit,
- (ii) State the basis (as defined in paragraph (b)(1) of this section) and the date of acquisition of the unit,
- (iii) Enumerate for each unit the amount of all expenditures incurred in connection with rehabilitation of such unit which would, but for section 263 (e) or (f), be properly chargeable to capital account (including expenditures incurred by the taxpayer in connection with rehabilitation of such unit undertaken by a person other than the taxpayer) regardless of whether such expenditures during any 12-month period exceed 20 percent of the basis of such unit,
- (iv) Describe the nature of the work in connection with each expenditure, and
- (v) Specify the calendar month in which the rehabilitation is completed and the taxable year in which each expenditure is paid or incurred.

A section 263(e) record need only be prepared for a unit of railroad rolling stock for the period beginning on the first day of the eleventh calendar month immediately preceding the month in which the rehabilitation of such unit is completed and ending on the last day of the eleventh calendar month immediately succeeding such month. No section 263(e) record need be prepared for calendar months before January 1970.

(3) *Records for certain expenditures:* Expenditures determined to be incidental repairs and maintenance (referred to in paragraph (c) of this section) shall not be entered in the section 263(e) record. However, each taxpayer shall maintain records to reflect that such expenditures are properly deductible.

(4) *Convenience rule.* In general, expenditures and information maintained in compliance with subparagraphs (1) and (2) of this paragraph shall be recorded in the section 263(e) record of the specific unit with respect to which such expenditures are incurred. However, when a group of units of the same type are rehabilitated in a single project and the expenditure for each unit in the project will approximate the average expenditure per unit for

the project, expenditures for the project may be aggregated without regard to the unit in the project with respect to which each expenditure is connected, and an amount equal to the aggregate expenditures for the project divided by the number of units in the project may be entered in the section 263(e) account of each unit in the project.

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

*Example 1.* M Corporation, a domestic common carrier by railroad, uses the calendar year as its taxable year. M owns and uses several gondola cars to which an election under section 263(e) applies for its taxable years 1970-1972. Gondola car No.1 has a basis (defined in paragraph (b)(1) of this section) of \$10,000. No expenditures properly chargeable to the section 263(e) record are made on gondola car No. 1 in 1970 and 1971, except in January 1971. In January 1971, M at a cost of \$1,500 performed rehabilitation work on gondola car No. 1. Such amount was properly entered in the section 263(e) record for gondola car No.1. Since the expenditures in such record do not exceed an amount equal to 20 percent of the basis of gondola car No. 1 (\$2,000) during any period of 12 calendar months in which January 1971 falls, the expenditures during January 1971 shall be treated as a deductible expense regardless of what the treatment would have been if section 263(e) had not been enacted.

*Example 2.* Assume the same facts as in *Example (1)*. Assume further that for 1970, 1971, and 1972, only the following expenditures in connection with rehabilitation which would, but for section 263(e), be properly chargeable to capital account were deemed included for gondola car No. 2:

(a) December 1970 .....	\$1,500
(b) November 1971 .....	600
(c) December 1971 .....	400
(d) January 1972 .....	1,050

Assume further that gondola car No. 2 has a basis (as defined in paragraph (b) (1) of this section) equal to \$10,000, that M files its tax return by September 15 following each taxable year, and that each rehabilitation was completed in the month in which expenditures in connection with it were incurred. Any expenditures in connection with each gondola car (No. 1 or No. 2) have no effect on the treatment of expenditures in connection with the other gondola car. With respect to gondola car No. 2, the expenditures of December 1970 are treated as deductible repairs at the time M's income tax return for 1970 is filed because, based on the information available when the income tax return for

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1970 is filed, such expenditure would be deductible by reason of application of section 263(e) but for the fact that it cannot be established whether the 20-percent limitation in paragraph (d)(1) of this section will be exceeded. Nevertheless, because such expenditures during the period of 12 calendar months including calendar months December 1970 and November 1971 exceed \$2,000, the December 1970 rehabilitation expenditures are not subject to the provisions of section 263(e). Because such rehabilitation expenditures during the period of 12 calendar months including calendar months February 1971 and January 1972 exceed \$2,000, rehabilitation expenditures in 1971 are not subject to the provisions of section 263(e). Similarly, the 1972 rehabilitation expenditures are not subject to the provisions of section 263(e).

[T.D. 7257, 38 FR 4255, Feb. 12, 1973]

### § 1.263(f)-1 Reasonable repair allowance.

(a) For rules regarding the election of the repair allowance authorized by section 263(f), the definition of repair allowance property, and the conditions under which an election may be made, see paragraphs (d) (2) and (f) of § 1.167(a)-11. An election may be made under this section for a taxable year only if the taxpayer makes an election under § 1.167(a)-11 for such taxable year.

(Sec. 263(f), 85 Stat. 509 (26 U.S.C. 263))

[T.D. 7272, 38 FR 9986, Apr. 23, 1973; 38 FR 12919, May 17, 1973; as amended by T.D. 7593, 44 FR 5421, Jan. 26, 1979]

### § 1.263A-0 Outline of regulations under section 263A.

This section lists the paragraphs in §§ 1.263A-1 through 1.263A-4 and §§ 1.263A-7 through 1.263A-15 as follows:

#### § 1.263A-1 Uniform Capitalization of Costs.

- (a) Introduction.
  - (1) In general.
  - (2) Effective dates.
  - (3) General scope.
    - (i) Property to which section 263A applies.
    - (ii) Property produced.
    - (iii) Property acquired for resale.
    - (iv) Inventories valued at market.
    - (v) Property produced in a farming business.
    - (vi) Creative property.
    - (vii) Property produced or property acquired for resale by foreign persons.
- (b) Exceptions.
  - (1) Small resellers.
  - (2) Long-term contracts.

- (3) Costs incurred in certain farming businesses.
- (4) Costs incurred in raising, harvesting, or growing timber.
- (5) Qualified creative expenses.
- (6) Certain not-for-profit activities.
- (7) Intangible drilling and development costs.
- (8) Natural gas acquired for resale.
  - (i) Cushion gas.
  - (ii) Emergency gas.
- (9) Research and experimental expenditures.
- (10) Certain property that is substantially constructed.
- (11) Certain property provided incident to services.
  - (i) In general.
  - (ii) Definition of services.
  - (iii) De minimis property provided incident to services.
- (12) De minimis rule for certain producers with total indirect costs of \$200,000 or less.
- (13) Exception for the origination of loans.
- (c) General operation of section 263A.
  - (1) Allocations.
  - (2) Otherwise deductible.
  - (3) Capitalize.
  - (4) Recovery of capitalized costs.
- (d) Definitions.
  - (1) Self-constructed assets.
  - (2) Section 471 costs.
    - (i) In general.
    - (ii) New taxpayers.
    - (iii) Method changes.
  - (3) Additional section 263A costs.
  - (4) Section 263A costs.
- (e) Types of costs subject to capitalization.
  - (1) In general.
  - (2) Direct costs.
    - (i) Producers.
      - (A) Direct material costs.
      - (B) Direct labor costs.
    - (ii) Resellers.
  - (3) Indirect costs.
    - (i) In general.
    - (ii) Examples of indirect costs required to be capitalized.
      - (A) Indirect labor costs.
      - (B) Officers' compensation.
      - (C) Pension and other related costs.
      - (D) Employee benefit expenses.
      - (E) Indirect material costs.
      - (F) Purchasing costs.
      - (G) Handling costs.
      - (H) Storage costs.
      - (I) Cost recovery.
      - (J) Depletion.
      - (K) Rent.
      - (L) Taxes.
      - (M) Insurance.
      - (N) Utilities.
      - (O) Repairs and maintenance.
      - (P) Engineering and design costs.
      - (Q) Spoilage.
      - (R) Tools and equipment.