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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

TD 9147

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Time and Manner of Making §163(d)(4)(B) Election to Treat Qualified Dividend Income as Investment Income

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to an election that may be made by noncorporate taxpayers to treat qualified dividend income as investment income for purposes of calculating the deduction for investment interest. The regulations reflect changes to the law made by the Jobs and Growth Tax Relief Reconciliation Act of 2003. The regulations affect taxpayers making the election under section 163(d)(4)(B) to treat qualified dividend income as investment income. The text of these temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in the Proposed Rules section in this issue of the **Federal Register**.

DATES: Effective Date: These regulations are effective August 5, 2004.

Applicability Dates: For dates of applicability, see §1.163(d)-1T(d).

FOR FURTHER INFORMATION CONTACT: Amy Pfalzgraf, (202) 622-4950 (not a toll-free

number).

SUPPLEMENTARY INFORMATION:

**Background and Explanation of Provisions**

Section 163(d)(1) provides that the investment interest deduction for a noncorporate taxpayer for any taxable year is limited to the net investment income of the taxpayer for the taxable year. Section 163(d)(4)(A) defines “net investment income” as the excess of investment income over investment expenses. Section 163(d)(4)(B)(iii) provides that an electing taxpayer may take all or a portion of certain net capital gain attributable to dispositions of property held for investment into account as investment income. Section 1(h)(2) provides that any net capital gain taken into account as investment income is not eligible to be taxed at the capital gains rates.

Section 302(b) of the Jobs and Growth Tax Relief Reconciliation Act of 2003, (Public Law 108-27, 117 Stat. 762) (JGTRRA 2003), amended section 163(d)(4)(B) to provide that an electing taxpayer may take all or a portion of qualified dividend income (as defined in section 1(h)(11)(B)) into account as investment income. Section 302(a) of JGTRRA 2003 added new section 1(h)(11)(D) to provide that any qualified dividend income taken into account as investment income is not eligible to be taxed at the capital gains rates.

Section 1.163(d)-1 of the Income Tax Regulations provides rules regarding the time and manner for making the net capital gain election under section 163(d)(4)(B)(iii). These regulations amend §1.163(d)-1 to provide that the rules regarding the time and manner for

making the qualified dividend income election under section 163(d)(4)(B)

are the same as the rules for making the net capital gain election under section 163(d)(4)(B)(iii).

### **Special Analyses**

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. For application of the Regulatory Flexibility Act (5 U.S.C. chapter 6) please refer to the cross-reference notice of proposed rulemaking published elsewhere in this issue of the Federal Register. Pursuant to section 7805(f) of the Internal Revenue Code, these temporary regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

### **Drafting Information**

The principal author of these regulations is Amy Pfalzgraf of the Office of Associate Chief Counsel (Income Tax & Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

### **List of Subjects in 26 CFR Part 1**

Income taxes, Reporting and recordkeeping requirements.

### **Amendments to the Regulations**

Accordingly, 26 CFR part 1 is amended as follows:

Part 1--INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read, in part, as follows:

Authority: 26 U.S.C. 7805 \* \* \*

Par. 2. Section 1.163(d)-1 is revised.

§1.163(d)-1 Time and manner for making elections under the Omnibus Budget

Reconciliation Act of 1993 and the Jobs and Growth Tax Relief Reconciliation Act of 2003.

(a) [Reserved]. For further guidance, see §1.163(d)-1T(a).

(b) [Reserved]. For further guidance, see §1.163(d)-1T(b).

(c) [Reserved]. For further guidance, see §1.163(d)-1T(c).

(d) [Reserved]. For further guidance, see §1.163(d)-1T(d).

Par. 3. Section 1.163(d)-1T is added to read as follows:

§1.163(d)-1T Time and manner for making elections under the Omnibus Budget

Reconciliation Act of 1993 and the Jobs and Growth Tax Relief Reconciliation Act of 2003

(temporary).

(a) Description. Section 163(d)(4)(B)(iii), as added by section 13206(d) of the Omnibus Budget Reconciliation Act of 1993 (Public Law 103-66, 107 Stat. 467), allows an electing taxpayer to take all or a portion of certain net capital gain attributable to dispositions of property held for investment into account as investment income. Section 163(d)(4)(B), as amended by section 302(b) of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (Public Law 108-27, 117 Stat. 762), allows an electing taxpayer to take all or a portion of qualified dividend income, as defined in section 1(h)(11)(B), into account as investment income. As a consequence, the net capital gain and qualified

dividend income taken into account as investment income under these elections are not eligible to be taxed at the capital gains rates. An election may be made for net capital gain recognized by noncorporate taxpayers during any taxable year beginning after December 31, 1992. An election may be made for qualified dividend income received by noncorporate taxpayers during any taxable year beginning after December 31, 2002, but before January 1, 2009.

(b) Time and manner for making the elections. The elections for net capital gain and qualified dividend income must be made on or before the due date (including extensions) of the income tax return for the taxable year in which the net capital gain is recognized or the qualified dividend income is received. The elections are to be made on Form 4952, "Investment Interest Expense Deduction," in accordance with the form and its instructions.

(c) Revocability of elections. The elections described in this section are revocable with the consent of the Commissioner.

(d) Effective date. The rules set forth in this section regarding the net capital gain election are effective December 12, 1996. The rules set forth in this section regarding the qualified dividend income election apply to any taxable year beginning

after December 31, 2002, but before January 1, 2009.

Nancy J. Jardini,  
Acting Deputy Commissioner for Services and Enforcement.

Approved: July 29, 2004

Gregory F. Jenner,  
Acting Assistant Secretary of the Treasury.