



Questions and answers about the limitation on the deduction for business interest expense

FS-2025-09, Dec. 2025

This Fact Sheet issues frequently asked questions about the limitation on the deduction for business interest expense.

These FAQs are being issued to provide general information to taxpayers and tax professionals as expeditiously as possible. Accordingly, these FAQs may not address any particular taxpayer's specific facts and circumstances, and they may be updated or modified upon further review. Because these FAQs have not been published in the Internal Revenue Bulletin, they will not be relied on or used by the IRS to resolve a case. Similarly, if an FAQ turns out to be an inaccurate statement of the law as applied to a particular taxpayer's case, the law will control the taxpayer's tax liability. Nonetheless, a taxpayer who reasonably and in good faith relies on these FAQs will not be subject to a penalty that provides a reasonable cause standard for relief, including a negligence penalty or other accuracy-related penalty, to the extent that reliance results in an underpayment of tax. Any later updates or modifications to these FAQs will be dated to enable taxpayers to confirm the date on which any changes to the FAQs were made. Additionally, prior versions of these FAQs will be maintained on IRS.gov to ensure that taxpayers, who may have relied on a prior version, can locate that version if they later need to do so.

More information about [reliance is available](#). These FAQs were announced in [IR-2025-126](#).

Background

Below are answers to some basic questions about the limitation on the deduction for business interest expense, also known as the "section 163(j) limitation." Prior to the 2017 Tax Cuts and Jobs Act (TCJA), section 163(j) of the Internal Revenue Code applied only to certain interest paid or accrued by corporations. However, the TCJA significantly changed the section 163(j) limitation. On March 27, 2020, section 163(j) was further amended by the Coronavirus Aid, Relief, and Economic Security Act (CARES Act). The Treasury Department and the IRS issued final regulations under section 163(j) in Sept. 2020 and Jan. 2021. See Treasury Decisions 9905 and 9943. Additionally, changes to section 163(j) were made as part of the One, Big, Beautiful Bill (P.L. 119-21). Some of the changes apply to tax years beginning after Dec. 31, 2024, while other changes become effective for tax years beginning after Dec. 31, 2025.

These questions and answers address the section 163(j) limitation after amendments by the TCJA, the CARES Act, and the One, Big, Beautiful Bill.

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Topic A: General

Q1. What is the section 163(j) limitation on the deduction for business interest expense? (updated Dec. 23, 2025)



A1. Generally, taxpayers can deduct interest expense paid or accrued in the taxable year. However, if the section 163(j) limitation applies, the amount of deductible business interest expense in a taxable year cannot exceed the sum of:

1. The taxpayer's business interest income for the taxable year;
2. 30% of the taxpayer's adjusted taxable income (ATI) for the taxable year; and
3. The taxpayer's floor plan financing interest expense for the taxable year.

Under the CARES Act, a different percentage (50%) of ATI may apply for taxable years beginning in 2019 and 2020. See the CARES Act, discussed later, and [Revenue Procedure 2020-22](#), for ATI elections and special rules for partnerships.

Q2. Who is subject to the section 163(j) limitation? (updated Jan. 10, 2023)

A2. For taxable years beginning after Dec. 31, 2017, the limitation applies to all taxpayers who have business interest expense, other than certain small businesses that meet the gross receipts test in section 448(c) ("exempt small business") (see [Topic A: Q 3-4](#)). The limitation does not apply to certain electing trades or businesses and certain excepted trades or businesses (see [Topic B: Q 1-2](#)).

Q3. What is the gross receipts test for purposes of the section 163(j) limitation? (updated Dec. 23, 2025)

A3. A business generally meets the gross receipts test of section 448(c) for a taxable year when it is not a tax shelter (as defined in section 448(d)(3)) and has average annual gross receipts of \$25 million or less in the previous three years. The \$25 million gross receipts amount is adjusted annually for inflation. The inflation adjusted gross receipts amount for 2024 is \$30 million. The inflation adjusted gross receipts amount for 2025 is \$31 million.

Q4. My average annual gross receipts for years 2021-2023 were more than \$30 million subjecting me to a section 163(j) interest expense limitation for the 2024 tax year. A portion of that interest expense was limited and carried forward to 2025. If my average annual gross receipts based on tax years 2022 through 2024 decrease to below \$31 million, will I be subject to the section 163(j) limitation when I file for the 2025 taxable year? (updated Dec. 23, 2025)

A4. No. Although you were subject to the section 163(j) limitation for the 2024 taxable year, the limitation does not apply to you for the 2025 taxable year. The disallowed portion of business interest expense from 2024 that is carried forward to 2025, along with the amount of 2025 business interest, will not be subject to the limitation in 2025 because your average annual gross receipts for 2022-2024 is below \$31 million. Therefore, you do not need to compute the section 163(j) limitation for the 2025 taxable year.

Note: This answer assumes that you are operating only one trade or business that is not an electing or excepted trade or business, as discussed in [Topic B: Q 1-3](#) below.

Topic B: Excepted Trades or Businesses

Q1. Which businesses qualify as an excepted trade or business?

A1. The following are excepted trades or businesses:

- The trade or business of providing services as an employee;
- Certain real property trades or businesses that elect to be excepted;
- Certain farming businesses that elect to be excepted; and
- Certain regulated utility trades or businesses.



Q2. How does an eligible real property trade or business or farming business elect to be an excepted trade or business? (updated Jan. 10, 2023)

A2. A taxpayer with an eligible real property trade or business or farming business may make an election to be an excepted trade or business by following the procedures outlined in Treas. Reg. §1.163(j)-9, including the requirement to attach a statement to a timely filed federal income tax return (including any extensions) for the taxable year of election. See also Revenue Procedures [2018-59](#), [2020-22](#), and [2021-9](#). An exempt small business is permitted to make an election to be an excepted trade or business even though that taxpayer may already not be subject to the section 163(j) limitation. See Treas. Reg. §§1.163(j)-2(d)(1) and 1.163(j)-9(b). This provision is intended to allow taxpayers who are unsure whether they qualify as an exempt small business to make a protective election without having to apply the gross receipts test described in [Topic A: Q 1](#) above for the prior three taxable years. Once made, an election is generally irrevocable and binding on the trade or business for all succeeding years. See Treas. Reg. §1.163(j)-9 for certain circumstances where the election terminates. The statement making an election to be an excepted trade or business that is attached to the taxpayer's return for the taxable year of election must include the following information:

- The taxpayer's name, address, and social security number or employer identification number;
- A description of the electing trade or business, including the principal business activity code; and
- A statement that the taxpayer is making an election as a real property trade or business (under section 163(j)(7)(B) or as a farming business (under section 163(j)(7)(C)), as applicable.

Q3. Are there any consequences I should be aware of in making an election to be an excepted trade or business? (updated Jan. 10, 2023)

A3. Yes. If you make an election to be an excepted real property trade or business, the following assets that you hold in the electing real property trade or business must be depreciated using the alternative depreciation system (ADS) and are not eligible for a bonus depreciation deduction under section 168(k):

- Nonresidential real property;
- Residential rental property; and
- Qualified improvement property.

If you make an election to be an electing farming business, any property with a recovery period of 10 years or more that you hold in the electing farming business must be depreciated using ADS, and such property is not eligible for a bonus depreciation deduction under section 168(k). See Revenue Procedures [2019-08](#), [2020-22](#), [2020-25](#), and [2021-9](#) for more information.

Topic C: Determining the Section 163(j) Limitation Amount

Q1. What is considered interest for purposes of section 163(j)? (updated Jan. 10, 2023)

A1. Treas. Reg. §1.163(j)-1(b)(22) defines the term "interest" to determine interest expense and interest income for purposes of section 163(j). In general, under Treas. Reg. §1.163(j)-1(b)(22), interest is any amount that is paid, received, or accrued as compensation for the use or forbearance of money under the terms of an instrument or contractual arrangement, including a series of transactions, that is treated as a debt instrument for purposes of section 1275(a) and Treas. Reg. §1.1275-1(d), or any amount that is treated as interest under other provisions of the Code or the regulations thereunder. Treas. Reg. §1.163(j)-1(b)(22) provides additional information on what constitutes interest for purposes of section 163(j), including anti-avoidance rules and a list of other amounts treated as interest, such as certain amounts of bond premium, factoring income, and certain dividends from regulated investment companies.

Q2. What is business interest expense? (updated Dec. 23, 2025)



A2. Business interest expense is any interest expense that is properly allocable to a trade or business that is not an excepted trade or business.

For tax years beginning after Dec. 31, 2025, section 163(j) is applied before any mandatory or elective interest capitalization provisions, except for sections 263(g) and 263A(f). Accordingly, business interest expense for these years excludes any interest capitalized under section 263(g) and 263A(f) and includes all other business interest expense.

Floor plan financing interest expense is also business interest expense. See [Topic C: Q 1](#), for what is considered interest. See [Topic C: Q 8](#), if you have interest expense that is allocable to both an excepted trade or business and a non-excepted trade or business.

Q3. What is business interest income? (updated Jan. 10, 2023)

A3. Business interest income is interest income that is includable in gross income and properly allocable to a trade or business that is not an excepted trade or business. See [Topic C: Q 1](#), above, for what is considered interest. See [Topic C: Q8](#) if you have interest income that is allocable to both an excepted trade or business and a non-excepted trade or business.

Q4. How do I calculate ATI (ATI limitation)? (updated Dec. 23, 2025)

A4. ATI is calculated by taking the taxable income for the taxable year as if section 163(j) does not limit any interest deduction, and then adding and subtracting from that amount certain amounts for the taxable year:

Additions include, but are not limited to, business interest expense; net operating loss deduction; deduction for qualified business income under section 199A; depreciation, amortization, or depletion deduction for taxable years beginning before Jan. 1, 2022, and after Dec. 31, 2024; capital loss carrybacks or carryovers; and any deduction or loss not properly allocable to a non-excepted trade or business.

Subtractions include, but are not limited to, business interest income; floor plan financing interest expense; with respect to the sale or other disposition of property (which may take place in a taxable year starting on or after Jan. 1, 2022), the greater of the allowed or allowable depreciation, amortization or depletion of the property for taxable years beginning before Jan. 1, 2022, and after Dec. 31, 2024; and any income or gain that is not properly allocable to a non-excepted trade or business.

For taxable years beginning after Dec. 31, 2021, and before Jan. 1, 2025, deductions for depreciation, amortization, or depletion are not added back to taxable income in calculating ATI.

Certain other adjustments to ATI apply for some types of taxpayers. See Treas. Reg. §1.163(j)-1(b)(1).

Q5. How Do I Make the Election to Substitute Adjusted Taxable Income for the Last Taxable Year in 2019? (updated Dec. 23, 2025)

A5. The CARES Act allows a taxpayer to elect to substitute its ATI for the last taxable year beginning in 2019 for the taxpayer's ATI in determining the taxpayer's section 163(j) limitation for any taxable year beginning in 2020, subject to modifications for short taxable years.

If this election is made, complete line 22, adjusted taxable income, on [Form 8990](#) and leave lines 6 through 21 blank. No formal statement is required to make this election. Please see section 6.02 of [Revenue Procedure 2020-22](#) for additional information regarding this election under section 163(j)(10), as enacted by the CARES Act.



Q6. What is floor plan financing interest expense? (updated Dec. 23, 2025)

A6. Floor plan financing interest expense is interest paid or accrued on floor plan financing indebtedness. Floorplan financing indebtedness is indebtedness that is used to finance the acquisition of motor vehicles held for sale or lease and that is secured by the acquired inventory. For example, if you own an automobile dealership and pay interest on a loan that is secured by the dealership's office equipment, then such interest is not a floorplan financing interest expense since it is not secured by the acquired inventory.

For purposes of floor plan financing, a motor vehicle is defined as any one of the following:

- A self-propelled vehicle designed for transporting persons or property on a public street,
- A boat, and
- Farm machinery or equipment

For tax years beginning after Dec. 31, 2024, a motor vehicle also includes any trailer or camper which is designed to provide temporary living quarters for recreational, camping or seasonal use and is designed to be towed by, or affixed to, a motor vehicle.

Q7. What happens to business interest expense that I cannot deduct in the current year because of the section 163(j) limitation? (updated Dec. 23, 2025)

A7. The amount of business interest expense disallowed as a deduction in the current year under section 163(j) is carried forward to the next taxable year (a "disallowed business interest expense carryforward"). Your disallowed business interest expense carryforward may be limited in the next taxable year if the section 163(j) limitation continues to apply to you. Special rules apply to partnerships and S Corporations (see [Topic C: Q 9](#)). For taxable years beginning after Dec. 31, 2025, no portion of any business interest carried forward from any taxable year to any succeeding taxable year is treated as interest to which an interest capitalization provision applies. The term "interest capitalization provision" means any provision under which interest is required to be charged to a capital account or may be deducted or charged to a capital account.

Q8. If I'm engaged in both an excepted trade or business and a non-excepted trade or business, how do I determine the section 163(j) limitation? (updated Jan. 10, 2023)

A8. Your interest expense that is properly allocable to an excepted trade or business is not subject to the section 163(j) limitation. Similarly, the amount of your items of income, gain, deduction, or loss, including interest income that is properly allocable to an excepted trade or business, is excluded in determining the section 163(j) limitation. Therefore, you should allocate tax items between excepted and non-excepted trades or businesses in order to determine the section 163(j) limitation. Treas. Reg. §1.163(j)-10 provides special rules for allocating various tax items. You must generally compare your basis in the assets you use in your excepted trades or businesses and your basis in the assets you use in your non-excepted trades or businesses to determine what portion of interest expense and interest income to allocate to your excepted trades or businesses. In limited cases, tracing of interest expense paid on certain non-recourse debt may be available.

Q9. How does the section 163(j) limitation apply to partnerships and S corporations? (updated Jan. 10, 2023)

A9. The section 163(j) limitation is applied at the partnership level. As provided in [Topic A: Q 1](#), the amount of deductible business interest expense in a taxable year cannot exceed the sum of the



partnership's business interest income, 30% of the partnership's ATI, and the partnership's floor plan financing interest expense.

Business interest expense that may be deducted upon application of the section 163(j) limitation is taken into account in determining the non-separately stated taxable income or loss of the partnership. Any business interest expense of the partnership that is disallowed upon application of the section 163(j) limitation is allocated to each partner in the same manner as the non-separately stated taxable income or loss of the partnership. This amount is called excess business interest expense (EBIE).

A partner carries forward its share of EBIE. In a succeeding taxable year, a partner may treat its EBIE as business interest expense paid or accrued by the partner to the extent the partner is allocated excess taxable income or excess business interest income from the same partnership. Excess taxable income is the amount of ATI of the partnership that was in excess of what it needed to deduct its business interest expense. Excess business interest income is the amount by which business interest income exceeded business interest expense at the partnership level. Excess taxable income is allocated to each partner in the same manner as the non-separately stated taxable income or loss of the partnership. An allocation of excess taxable income to a partner increases the partner's ATI. Similarly, an allocation of excess business interest income to a partner increases the partner's business interest income. Once EBIE is treated as business interest expense paid or accrued by the partner, such business interest expense is subject to the partner's section 163(j) limitation, if any (see [Topic A: Q 1](#)).

S corporations apply the section 163(j) limitation at the S corporation level. Any business interest expense of the S corporation that is disallowed upon application of the section 163(j) limitation is not allocated to its shareholders but is instead carried over at the S corporation level to its succeeding taxable years. An S corporation allocates any excess taxable income and excess business interest income to its shareholders on a pro-rata basis.

Treas. Reg. §1.163(j)-6 provides special rules and defined terms relating to the application of section 163(j) to partnerships and S corporations. Treas. Reg. §1.163(j)-6(f)(2) specifically sets out the steps for allocating deductible business interest expense and the section 163(j) excess items for partnerships.

For taxable years beginning in 2020 only, a partner (unless it elects out) may treat 50% of its allocable share of a partnership's EBIE for 2019 as an interest deduction for 2020 without limitation. The remaining 50% of the partnership's EBIE for 2019 remains subject to the section 163(j) limitation applicable to the EBIE carried forward at the partner level. See [Revenue Procedure 2020-22](#) for rules for partnerships under the CARES Act. For additional discussion of CARES Act changes see [Topic D: Q 2](#).

Q10. How does a partner account for business interest expense when it computes its section 704(d) basis loss limitation? (added Jan. 10, 2023)

A10. Treas. Reg. §1.163(j)-6(h) provides for a separate section 704(d) loss class for business interest expense comprised of: deductible business interest expense and business interest expense of an exempt entity (whether allocated to the partner in the current taxable year or suspended under section 704(d) in a prior taxable year), any excess business interest expense (EBIE) allocated to the partner in the current taxable year, and any EBIE from a prior taxable year that was suspended under section 704(d) (negative section 163(j) expense).

After the partner determines the amount of the limitation apportioned to this section 704(d) loss class, any deductible business interest expense is taken into account before any EBIE or negative section 163(j) expense. See Example 7 in Treas. Reg. §1.163(j)-6(o)(7) for more information.

This provision is generally applicable for taxable years beginning on or after Nov. 13, 2020. For more information, see the applicability date in Treas. Reg. §1.163(j)-6(p).



Q11. How does the section 163(j) limitation apply to a consolidated group of corporations? (updated Jan. 10, 2023)

A11. The section 163(j) limitation applies at the consolidated return level, and a consolidated group has a single limitation. In calculating the limitation, a consolidated group's business interest expense and business interest income is, respectively, the sum of its members' business interest expense and business interest income. The consolidated group should calculate its ATI using the group's taxable income as determined under Treas. Reg. §1.1502-11 without regard to any carryforwards or disallowances under section 163(j).

Q12. Does the section 163(j) limitation apply to foreign corporations? (updated Jan. 10, 2023)

A12. Yes, the section 163(j) limitation applies to any foreign corporation whose classification is relevant under Treas. Reg. §301.7701-3(d)(1) for a taxable year other than solely pursuant to section 881 or 882. As a result, section 163(j) applies to any foreign corporation that is a controlled foreign corporation (CFC). Generally, section 163(j) applies to a CFC in the same manner as it applies to a domestic C corporation. If a CFC is a partner in a partnership, the section 163(j) limitation applies to the partnership in the same manner as if the CFC were a domestic C corporation. Treas. Reg. §1.163(j)-7 provides rules for determining the amount of ATI and calculating the limitation for CFCs.

If a CFC group election is in effect, a single section 163(j) limitation is computed for the CFC group under rules provided in Treas. Reg. §1.163(j)-7(c). In addition, if a CFC or CFC group is eligible for a safe-harbor election, none of the CFC's or CFC group members' business interest expense is disallowed in a taxable year for which the election is made.

Section 163(j) also applies to any foreign corporation (or other foreign person) that is engaged in a U.S. trade or business. Prop. Reg. §1.163(j)-8 provides rules for determining the amount of ATI and calculating the limitation for the foreign corporation (or other foreign person). In the case of a foreign corporation engaged in a U.S. trade or business, the proposed regulations coordinate the application of section 163(j) with the rules for allocating interest expense to income effectively connected with a U.S. trade or business.

Topic D: CARES Act Changes

Q1. What temporary changes were made under the CARES Act? (added Jan. 10, 2023)

A1. The CARES Act amended section 163(j) to provide benefits to taxpayers. See [Topic C: Q 9](#) and [Topic D: Q 2](#) for special rules for partnerships and its partners.

The CARES Act:

Retroactively increases the ATI percentage for taxable years beginning in 2019 and 2020 to 50% (rather than 30%). A taxpayer can elect not to apply the 50% ATI limitation and use the 30% ATI limitation instead. The election is made by filing a return using the 30% ATI limitation instead of the 50% ATI limitation. No formal statement is required to be attached to the return. See [Revenue Procedure 2020-22](#).

Allows a taxpayer to elect to substitute the taxpayer's 2019 ATI for the 2020 ATI in determining the taxpayer's section 163(j) limitation for taxable years beginning in 2020.

Q2. What temporary changes were made under the CARES Act for Partnerships and its Partners? (added Jan. 10, 2023)



A2. The CARES Act provides special rules for partnerships and partners:

For taxable years beginning in 2019, a partner treats 50% of its allocable share of a partnership's excess business interest expense (EBIE) for 2019 (2019 EBIE) as an interest deduction without limitation in the partner's first taxable year beginning in 2020 (50% EBIE rule). A partner may elect out of the 50% EBIE rule. The remaining 50% of such EBIE remains subject to the section 163(j) limitation rules applicable to EBIE carried forward at the partner level.

The 50% ATI limitation does not apply to partnerships for taxable years beginning in 2019.

A partnership may elect to use the 30% ATI limitation instead of 50% for only taxable years beginning in 2020. No formal statement is required to be attached to the return. See [Revenue Procedure 2020-22](#).

A partnership may elect to substitute the partnership's 2019 ATI for the 2020 ATI in determining the partnership's section 163(j) limitation for taxable years beginning in 2020. A partnership makes this election by timely filing Form 1065, including extensions, amended Form 1065 as appropriate or administrative adjustment request. No formal statement is required to be attached to the return. See [Revenue Procedure 2020-22](#).

Note: The CARES Act amendments discussed above only apply to taxable years beginning in 2019 and 2020 but do not apply to taxable years beginning in 2021 and later.

Q3. How does a taxpayer make an election under the CARES Act? (added Jan. 10, 2023)

A3. See [Revenue Procedure 2020-22](#) for more information on how to make an election.

Topic E: One, Big, Beautiful Bill changes

Q1. What changes were made under the One, Big, Beautiful Bill for tax years beginning after Dec. 31, 2024? (added Dec. 23, 2025)

A1. For tax years beginning after Dec. 31, 2024, the One, Big, Beautiful Bill amended section 163(j) to add back deductions for depreciation, amortization, or depletion to taxable income when calculating ATI. This change may benefit the taxpayer by increasing ATI allowing for a higher limitation amount on the calculation of business interest. Previously, for tax years beginning after Dec. 31, 2021, and before Jan. 1, 2025, these amounts were not allowed to be added back to taxable income in calculating ATI. See [Topic C: Q 4](#) for more details.

In addition, for tax years beginning after Dec. 31, 2024, the One, Big, Beautiful Bill amended section 163(j) with respect to floor plan financing interest expense to include, as a motor vehicle, any trailer or camper which is designed to provide temporary living quarters for recreational, camping or seasonal use and is designed to be towed by, or affixed to, a motor vehicle. See [Topic C: Q 6](#) for more information.

Q2. What changes were made under the One, Big, Beautiful Bill for tax years beginning after Dec. 31, 2025? (added Dec. 23, 2025)

A2. For tax years beginning after Dec. 31, 2025, section 163(j) is applied before any mandatory or elective interest capitalization provisions, except for sections 263(g) and 263A(f). Accordingly, business interest expense excludes any interest capitalized under section 263(g) and 263A(f) and includes all other business interest expense." See [Topic C: Q 2, 4 & 7](#) for more details.

Also, for tax years beginning after Dec. 31, 2025, the One, Big, Beautiful Bill amended section 163(j) to exclude a U.S. shareholder's CFC income inclusion items under sections 951(a), 951A(a) and 78



Fact Sheet

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Media Relations Office
Washington, D.C.

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Public Contact: 800.829.1040
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(including associated portions of deductions) from the computation of ATI. As a result of this change, a U.S. shareholder will no longer be allowed to increase its ATI by a portion of CFC income inclusions.

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